

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1963

No. 828

SECURITIES AND EXCHANGE COMMISSION,
PETITIONER,

vs.

AMERICAN TRAILER RENTALS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT
OF APPEALS FOR THE TENTH CIRCUIT

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Original Print

Record from the United States District Court for the District
of Colorado.

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1 Filed and Referred Concurrently, Jointly and Severally to Benjamin C. Hilliard, Jr., J. Gordon Bartley and Charles F. Keen, Referees in Bankruptcy.

December 20, 1962

G. Walter Bowman, Clerk
By AS
Deputy Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In the matter of
AMERICAN TRAILER RENTALS COMPANY, Debtor

In Proceedings for an Arrangement in Bankruptcy 33276

Petition for Arrangement—Filed December 20, 1962

To the Honorable Alfred A. Arraj
Chief Judge of the District Court of the
United States for the District of Colorado

The petition of American Trailer Rentals Company, 1825 Emerson Street, in the City and County of Denver, State of Colorado, and engaged in the renting of automobile utility trailers, respectfully represents:

1. Your petitioner is a business corporation organized and existing under the laws of the State of Colorado, and is a corporation which could become a bankrupt under the Act of Congress relating to bankruptcy and is not a municipal, railroad, insurance, or a banking corporation, or a building and loan association.
2. Your petitioner has had its principal place of business at 1825 Emerson Street, City and County of Denver, State of Colorado, and within the above judicial district for a longer portion of the six months immediately preceding the filing of this petition than in any other judicial district.
3. Within six years next preceding the filing of this petition, your petitioner has not been known and has not

conducted any business by or under any assumed, trade or other names or designations.

4. No bankruptcy proceeding initiated by a petition by or against your petitioner is now pending.

5. Your petitioner is unable to pay its debts as they mature.

6. Your petitioner proposes the arrangement with
2 its unsecured creditors which is annexed hereto and made a part hereof.

7. The schedule hereto annexed marked Schedule A and verified by your petitioner's oath contains a full and true statement of all its debts and so far as it is possible to ascertain, the names and places of residence of its creditors, and such further statements concerning said debts as are required by the provisions of the Act of Congress relating to bankruptcy.

AMERICAN TRAILER RENTALS COMPANY

/s/ IRVIN H. PETERS
Executive Vice-President of
said Corporation
Petitioner

/s/ GILBERT C. MAXWELL

/s/ BENJAMIN E. SWEET

2550 First National Bank Building

Denver 2, Colorado

AMherst 6-3558

Attorneys for Petitioner

*Duly sworn to by Irvin H. Peters
jurat omitted in printing*

3

Attachment to Petition

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In the matter of

AMERICAN TRAILER RENTALS COMPANY, Debtor

In Proceedings for An Arrangement

No.

PROPOSED ARRANGEMENT

The above named debtor, pursuant to Section 322, proposes the following arrangement with its unsecured creditors:

History of Debtor

The debtor was organized September 18, 1958, for the purpose of renting to the public automobile type utility trailers. It now rents approximately 3000 trailers of varying sizes for local use or one-way trips from one locality to another. The trailers are of all steel construction and are attached to the automobile of the renter, by means of a clamp-on bumper hitch which is a part of the trailer equipment. The trailers are rented to the public through a system of stations established by the debtor; there are now about 500 stations in the system. The rental fees vary according to the size of the trailer, and local use or one-way trips. The station operator collects the rental fee in advance, usually withholds his commission, and remits the balance of the fee to the debtor.

The debtor does not own the trailers. They are owned by individuals who paid the debtor for their manufacture. Certificates of Title to the trailers were issued by the manufacturer to the individuals who entered into leasing agreements with the debtor, providing for the rental of the trailers to the public. The trailers are now widely scattered throughout the country. The leasing agreements provide for payment to the trailer owners of a percentage of the amount paid to the debtor for the trailer; these percentages vary from 2% to 3% per month of this amount

4.
(a few provide for 35% of the rental derived by the trailers) and the leasing agreements have a remaining average term of eight years.

With respect to the 3000 trailers remaining in the system, the debtor has made payments to the trailer owners which, if treated as a return of capital to them, would leave a capital investment in these trailers of \$1,532,902.43. The debtor owes the trailer owners upon the leasing agreements the sum of \$710,597.53.

These leasing agreements, which created a fixed obligation of the debtor, are the primary cause of the present financial condition of the debtor.

Financial Condition of the Debtor

The amounts due upon the leasing agreements (executory contracts) total \$710,597.53. The debtor is also indebted to trailer owners for \$200,677.31, paid for trailers which were not manufactured; this amount was paid over by the debtor to the trailer manufacturer, DeMar, Inc., of Alliance, Nebraska, which company went into bankruptcy earlier this year. The debtor owes general creditors the sum of \$19,272.28. It is indebted to officers, directors and large stockholders on promissory notes, totaling \$285,277.00, for loans made by them to the debtor. The debtor was indebted to the Denver United States National Bank for \$50,000.00 on notes guaranteed by the officers of the debtor; the balance of this note has been reduced to \$40,000.00, by payment of the guarantors. Alexander Grant & Company has notes of the debtor, also guaranteed by officers of the debtor, amounting to \$15,557.95. It owes station operators \$10,833.70 — field employees \$6,691.97 — and it owes \$41,698.20 in connection with trailer replacement and repair. The debtor's only obligation to secured creditors is in the amount of \$5,611.68, for equipment and office furniture, subject to chattel mortgages.

The rentals which the debtor has received amount to approximately \$30,000.00 a month, during the summer months; in November, 1962, the amount of rentals received was about \$14,000.00.

Plan of Arrangement

It is realized that the method of operation of the debtor in paying to trailer owners a percentage of their cost of

the trailers' monthly was uneconomical and unsound; this method was initiated by the original promoters of the company, who preceded the present management. The plan of arrangement contemplates the assignment of titles to the trailers to a new corporation for shares 5 in the new corporation, as well as the transfer of the station rental system to the new corporation.

Capitol Leasing Corporation was organized on March 27, 1962, by one of the officers of the debtor and several trailer owners, for the purpose of offering its shares of stock for trailers operated by the debtor, as well as for trailers operated by other trailer rental companies. Capitol Leasing Corporation now owns 299 trailers, acquired in exchange for 88,332 shares of its no par value common stock. These trailers had an original cost of \$176,665.93, and the shares were issued on the basis of one share of stock for each \$2.00 invested in the trailers. The authorized capitalization of Capitol Leasing Corporation consists of 3,200,000 shares of no par value common stock, and Capitol has only the above number of shares outstanding.

The plan of arrangement is the issuance of shares of Capitol Leasing Corporation to trailer owners, upon assignment of titles to the trailers owned to Capitol Leasing Corporation, on the basis of one share of stock for each \$2.00 of the remaining capital investment in the trailers. The plan of arrangement also contemplates the issuance of shares of stock of Capitol Leasing Corporation, on the same basis, in satisfaction of the claims relating to trailers not manufactured; and the issuance of shares of Capitol Leasing Corporation stock to creditors of the debtor in satisfaction of their claims; and also, shares of stock of Capitol Leasing Corporation to be issued to the stockholders of the debtor for the assignment of the station rental system which was built by the debtor at an estimated cost of \$500,000.00. This plan has been approved by the Board of Directors of Capitol Leasing Corporation, subject to ratification by its forty (40) stockholders.

Provision for the Rejection of Executory Contracts

The executory contracts, namely, the leasing agreements, which provide for the payment by the debtor to trailer owners of percentages, monthly, based upon the cost of their

trailers, as well as monthly payments of a percentage of the rental derived through the renting of the trailers, which executory contracts are listed on Schedule A, are hereby rejected.

6 *Classification of Creditors*

Class I—shall be paid in full upon confirmation, the same being fees for Referees, salary fund and expense fund.

Class II—Such salaries and expenses as are necessary to continue the debtor in control and to preserve its assets, pending final confirmation of the plan.

Class III—Taxes legally due and owing shall be paid in full, upon confirmation of the plan.

Class IV—Cost and expenses of the proceedings, including attorneys fees, shall also be paid in full, upon confirmation of the plan.

Class V—Unsecured debts shall be paid and satisfied as follows:

- 1) The amounts due trailer owners, totaling \$710,597.53, shall be satisfied by the issuance of Capitol Leasing Corporation, upon receipt of Certificates of Title to the trailers, of one (1) share of its no par value common stock for each \$2.00 of the remaining capital investment in the trailers; if Certificates of Title to all the trailers are assigned to Capitol Leasing Corporation, a total of 766,451 shares will be issued by Capitol Leasing Corporation covering such assignments of trailer titles.
- 2) The issuance by Capitol Leasing Corporation of its shares of no par value common stock on the basis of one (1) share for each \$2.00 paid for trailers which were not manufactured, in the amount of \$200,677.31, or 100,388 shares.
- 3) The issuance by Capitol Leasing Corporation of its shares of no par value common stock to general creditors of the debtor on the basis of one (1) share for each \$3.50 of debt of the debtor. This includes the amount owed to officers, directors and stockholders for loans by them to the debtor, of \$285,277.00; to general

creditors, in the amount of \$19,272.28; to station operators, in the amount of \$10,833.70; to field representatives, in the amount of \$6,694.97; and for amounts payable in connection with trailer repair and replacement, in the amount of \$41,698.20—totaling \$361,773.15. This involves the issuance of a total of 103,935 shares.

7. 4) The satisfaction of the obligations to Denver United States National Bank, in the amount of \$40,000.00, and to Alexander Grant & Company, in the amount of \$15,557.95, by the refinancing of such obligations by Capitol Leasing Corporation in an amount sufficient to liquidate these obligations, to be secured by trailers owned by Capitol Leasing Corporation.

*Provision for Retention
of
Jurisdiction by the Court*

The Court shall retain jurisdiction until the confirmation of the plan, the delivery to and receipt by Capitol Leasing Corporation of Certificates of Title to trailers owned by those trailer owners desiring to participate in the plan, and the delivery of the shares of common stock of Capitol Leasing Corporation, as provided in the plan.

General Provisions

Capitol Leasing Corporation has agreed, within thirty (30) days after confirmation of this arrangement, to submit to the vote of its stockholders the ratification of the participation of Capitol Leasing Corporation in the plan, and also the issuance of 107,100 shares of its no par value common stock to the debtor for the assignment of the station rental system, for distribution to shareholders of the debtor.

The proponents of this plan believe that it is feasible—and submit that the adoption of the plan by trailer owners and creditors will allow Capitol Leasing Corporation and the debtor the opportunity to combine their resources with the result that the business operation may be carried on successfully. Unless the plan is adopted, proponents suggest that creditors will receive little, if anything, in settle-

ment of debtor's obligation to them, and that trailer owners may find themselves unable to realize any value for their trailers or any income from their operation.

DATED at Denver, Colorado, this 20th day of December, 1962.

AMERICAN TRAILER RENTALS COMPANY

By: IRVIN H. PETERS

Debtor

Irvin H. Peters

Executive Vice President

Subscribed and sworn to before me this 20 day of December, A.D. 1962.

ROBERT S. PALMES

[SEAL]

Notary Public

My Commission expires August 8, 1964.

8

(File endorsement omitted)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In Proceedings for an Arrangement

No. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor*.

**Motion of Securities and Exchange Commission to Dismiss—
Filed February 20, 1963**

Pursuant to Section 328 of Chapter XI of the Bankruptcy Act, the Securities and Exchange Commission respectfully moves that the above named proceedings under Chapter XI of the Bankruptcy Act be dismissed, unless the petition for arrangement be amended to comply with the requirements of Chapter X of the Bankruptcy Act, or unless a creditors' petition under Chapter X is filed, within ten days, or within such other period of time as may be fixed by this Court.

Said proceedings should have been originally brought under Chapter X of the Bankruptcy Act because the Debtor's circumstances and capital structure are such that the relief afforded by Chapter XI is inadequate to satisfy the needs to be served, as is more fully set forth in the Commission's memorandum in support of this motion filed herewith. All facts upon which this motion is based are contained in the record in this proceeding or in the Commission's Notice of Hearing, Consent to a Stop Order by American Trailer Rentals Company, the Temporary Suspension Order of Capitol Leasing Corporation, and the Prospectus filed by Debtor on December 11, 1961, all of which are attached hereto as Exhibits 1, 2, 3, and 4.

The Commission also moves that the Hearing to Confirm the Arrangement of American Trailer Rentals System scheduled for March 1, 1963 be stayed pending the determination of the Commission's motion herein.

The Commission requests that its Motion to Dismiss be heard by the Court upon such notice as may be directed pursuant to Section 328 of the Bankruptcy Act.

/s/ THOMAS B. HART

/s/ J. KIRK WINDLE

/s/ WILLIAM D. SCHEID

/s/ WILLIAM J. COONEY

*Attorneys for Securities and
Exchange Commission*

105 West Adams Street

Chicago 3, Illinois

CENTRAL 6-7390

Of Counsel:

DONALD J. STOCKING

Regional Administrator

Securities and Exchange Commission

802 Midland Savings Building

Denver 2, Colorado

Exhibit 1 to Motion

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

Nov. 27, 1962

File No. 2-19446

In the Matter of

AMERICAN TRAILER RENTALS COMPANY

**ORDER FIXING TIME AND PLACE OF HEARING UNDER SECTION
8(d) OF THE SECURITIES ACT OF 1933, AS AMENDED, AND
DESIGNATING AN OFFICER TO TAKE TESTIMONY**

I

The Commission having reasonable cause to believe that the registration statement filed under the Securities Act of 1933, as amended, by Registrant on December 11, 1961 on Form S-1, includes untrue statements of material facts and omits to state material facts required to be stated therein, or necessary to make the statements therein not misleading, as more specifically set forth in the Statement of Matters to be considered pursuant to Section 8(d) of the Securities Act of 1933, as amended, which Statement of Matters is incorporated herein by reference and made a part hereof;

IT IS ORDERED that a hearing be held in such matter, pursuant to the provisions of Section 8(d) of the Securities Act of 1933, as amended, such hearing to be commenced at 10:00 A.M. M.S.T. on December 10, 1962 at the Denver Regional Office of the Commission, 802 Midland Savings Building, 444 17th Street, Denver 2, Colorado, and to continue thereafter at such time and place as the officer herein-after designated may determine;

IT IS FURTHER ORDERED that Sidney Gross, an officer of the Commission, or such other officer as the Commission may designate, be and he hereby is designated to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda or other

records deemed relevant or material to the inquiry, and to perform all other duties in connection therewith authorized by law.

By the Commission.

/s/ Orval L. DuBois
Orval L. DeBois
Secretary

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UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

Nov. 27, 1962

File No. 2-19446

In the Matter of

The Registration Statement of
AMERICAN TRAILER RENTALS COMPANY

Section 8(d)
Securities Act of 1933

STATEMENT OF MATTERS TO BE CONSIDERED AT A HEARING
PURSUANT TO SEC. 8(d) OF THE SECURITIES ACT OF 1933,
AS AMENDED

The registration statement filed December 11, 1961 on Form S-1 under the Securities Act of 1933, as amended, appears to include untrue statements of material facts and omits to state material facts required to be stated therein or necessary to make the statements therein not misleading, as more particularly set forth below:

I

*Cover Page, Introductory Statement, Distribution Spread
and Plan of Distribution (Items 1 and 2)*

A. The adequacy and accuracy of statements made on the Cover Page and in the prospectus under the caption "Introductory", and with respect to distribution spread and the plan of distribution, in view of the failure to disclose, among other things:

- (a) the speculative nature of the inherent risk involved in the purchase of such securities and the particular risks to be borne by the purchasers of the securities proposed to be offered, in view of the inability of the registrant to meet its obligations under presently outstanding trailer investments contracts from trailer rental income, together with a statement of the reasons therefore,
- 12 (b) the nature and amount of underwriting commissions to be received by officers, directors and salesmen of the registrant, and the net amount of proceeds to be received by the registrant.

B. The failure to disclose in a clear and concise manner in the forepart of the prospectus material facts regarding:

- (a) the history of the registrant and the hazards of the enterprise, particularly in view of the failure to disclose: (1) the sale of trailer purchase and lease agreements to the public at prices in excess of the cost of the trailers to the registrant and the use of such excess payments as a source of funds to meet contractual obligations for payments to purchasers of trailer purchase and lease agreements; (2) the inadequacy of the rental proceeds to defray operating costs as well as contractual obligations under lease agreements; and (3) the extensive amount of losses sustained by American Trailer Rentals Company (ATR), and the reasons therefor,
- (b) the formation by affiliates of ATR, including an officer and director, of a new corporation to offer stock to present and future ATR trailer owners in exchange for trailers for the purpose of reorganizing ATR and relieving it of the financial burden caused by its inability to meet contractual obligations made to trailer owners,
- (c) the extent of ATR's liability under the Securities Act of 1933, as amended, for sale of unregistered securities.

II

Use of Proceeds (Item 3)

A. The adequacy and accuracy of the disclosures with respect to the purposes for which the proceeds of the offering will be used and the amounts necessary to be used for each purpose, more particularly as follows:

- (a) the necessity for obtaining funds from the sales of securities covered by the registration statement, and using a portion of the proceeds to be received by ATR to make payments on trailer contractual obligations previously incurred and to be incurred through this offering, and
- (b) the necessity of obtaining a substantial amount of funds from other sources to make the payments referred to in subparagraph (a) above.

III

Summary of Operations (Item 6)

The failure of the Summary of Operations to meet the requirement of Instruction A.2. of the Instructions as to Financial Statements of Form S-1, in that Alexander Grant & Company, ATR's independent accountants, were unable to express an over-all opinion as to the Combined Statement of Operations due to the inadequacy of ATR's accounting records.

IV

*Business of the Company, History of the Company
(Items 9 and 11)*

A. The adequacy and accuracy of disclosures in the prospectus with respect to (1) the business of ATR, and (2) the history of ATR, more particularly with respect to, among others, the matters set forth below:

- (a) The statement that ATR has entered into agreements with approximately 700 station operators in the principal cities of the country,
- (b) The failure to disclose that the registrant has no agreements with station operators in New England

or New York City and agreements with only one or two operators in most of the other principal metropolitan areas east of Chicago,

14 (c) The statement that ATR rents trailers to the public through approximately 700 station operators scattered throughout the country and the failure to disclose that (i) the major portion of ATR's fleet is located in the western and midwestern states, (ii) due to the location of De Mar, Inc. (an affiliate of ATR, organized to manufacture trailers), no trailers were ever shipped east of Chicago, (iii) many of its station operators have only one trailer available for rental, causing a number of the station operators to cancel their agreements with ATR and (iv) ATR has been receiving requests from trailer owners to withdraw their trailers from the system,

(e) The statement that ATR is a self-insurer with respect to theft, damage or destruction to trailers, and the failure to disclose that by virtue of the financial condition of ATR, it is wholly unable to pay claims on such insurance,

(d) The statement that ATR may have cause of action against the trailer manufacturer for loss of rental income because of defective trailers and the failure to disclose all the facts concerning the affiliation between ATR and De Mar, Inc., the trailer manufacturer,

(e) The financial condition of De Mar, Inc. and its ability to perform under the exclusive manufacturing agreement of November 17, 1960, with ATR,

(f) The failure to disclose that ATR has been unable to secure 1962 licenses for a large number of its trailers due to lack of funds,

(g) The failure to disclose that ATR has inadequate maintenance facilities,

(h) The failure to set forth fully and completely the various and sundry defects in a large segment of ATR's trailer fleet,

- (i) The failure to disclose ATR's lack of zone or regional management and the effect thereof upon its operations,
- (j) The use by one or more of ATR's promoters of funds raised from the public for other than corporate business and the failure to apply such funds to the purchase of trailers,
- (k) The failure to set forth clearly and concisely any usage figures with respect to ATR's trailers fleet, including the average rental income per trailer and the average number of days each trailer was rented.

B. The accuracy and adequacy of the disclosure concerning the organization of Executive Sales Company, (Executive Sales) and the separate state companies, the purposes and function of such corporations and their relationship to the registrant.

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V

Interest of Management and Others in Certain Transactions (Item 20)

A. The omission of information from the prospectus concerning the interest and affiliation of management; particularly with respect to:

- (a) The failure to disclose the nature and amount of the interest of officers, directors and promoters of ATR in affiliates, particularly Executive Sales and separate corporations formed in certain states, the cost of their interest in such corporations, and the basis for determining the amount of securities of ATR received by them upon the merger of such companies into ATR;
- (b) The failure to disclose that I. H. Peters, an officer and director of ATR was a director, stockholder and sales representative of De Mar, Inc.,
- (c) The failure to disclose I. H. Peters' activities as sales representative for ATR and Executive Sales, and the amount of his interest in trailer sales on behalf of ATR and Executive Sales,

- (d) The failure to disclose W. N. Marks' position as both a director of ATR, and an officer and director of Executive Sales,
- (e) The failure to disclose the nature and amount of I. H. Peters' and W. N. Marks' interest in transactions between ATR and Executive Sales and De Mar, Inc.,
- (f) The failure to disclose all the circumstances under which I. H. Peters and W. N. Marks acquired their positions with ATR and Executive Sales,
- (g) The failure to disclose the amount of the interest of officers and directors of ATR in sales of trailer purchase and lease agreements on behalf of ATR and Executive Sales,
- (h) The failure to disclose that four of ATR's ten directors listed in the prospectus were elected at the request of W. N. Marks pursuant to an arrangement with I. H. Peters and others,

16 B. The adequacy and accuracy of information in the prospectus concerning any agreements or arrangements between ATR and its officers and directors with respect to loans made or to be made by such officers and directors of ATR.

Exhibit 2 to Motion

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

In the Matter of
AMERICAN TRAILER RENTALS COMPANY

File No. 2-19446

**CONSENT TO STOP ORDER, STIPULATION OF THE RECORD IN THE
PROCEEDINGS, WAIVER OF POST-Hearing PROCEDURES**

Whereas, on November 27, 1962, the Commission entered an order under Section 8(d) of the Securities Act of 1933, as amended, to determine whether or not a stop-order should issue thereunder suspending the effectiveness of the registration statement filed by American Trailer Rentals Company (Registrant), as set forth in the Statement of Matters incorporated in said order; and

The Registrant, therefore, stipulates as follows:

1. The Registrant hereby agrees that the Statement of Matters dated November 27, 1962, shall be taken as correct for the purpose of this hearing and for no other purpose, and serve as a part of the record upon which the Commission may enter a stop-order pursuant to Section 8(d) of the Securities Act of 1933, as amended, and hereby waives further hearings and proceedings;
2. The Registrant consents to having a stop-order entered by the Commission pursuant to Section 8(d) of the Securities Act of 1933, as amended, upon the basis of the record;
3. The Registrant waives the requirement of a recommended decision by the hearing officer;
4. The Registrant agrees that the staff of the Division of Corporation Finance may assist in the preparation of the Commission's opinion and all separation of functions between the Commission and the members of the staff participating in this matter are hereby waived;

18 5. The registrant waives all post-hearing procedures, including the filing of proposed findings of fact, conclusions of law, briefs and oral argument.

Executed this day of 1963.

AMERICAN TRAILER RENTALS COMPANY

By IRVIN H. PETERS

Irvin H. Peters

Executive Vice President

By GILBERT C. MAXWELL,

Gilbert C. Maxwell

By ARTHUR W. BURKE, JR.

Arthur W. Burke, Jr.

*Counsel for American Trailer
Rentals Company*

AGREED AND ACCEPTED:

DIVISION OF CORPORATION FINANCE

By JEREMIAH J. BRESNAHAN

Jeremiah J. Bresnahan

By GEORGE H. PARSONS

George H. Parsons

Staff Attorneys

Exhibit 3 to Motion

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

Oct. 9, 1962.

In the Matter of

CAPITOL LEASING CORPORATION

1123 Delaware Street
Denver 4, Colorado

File No. 24D-2578

Securities Act of 1933
Section 3(b) and Regulation A

ORDER TEMPORARILY SUSPENDING EXEMPTION, STATEMENTS OF
REASONS THEREFOR, AND NOTICE OF OPPORTUNITY FOR
HEARING

I

Capitol Leasing Corporation (issuer) filed a notification and offering circular on May 7, 1962, relating to a proposed offering of 150,000 shares of its no par value common stock at \$2 per share or, in the alternative, in exchange for the assignment to the issuer of automobile-type utility trailers on the basis of one share of common for each \$2 of the cost of the trailer assigned to the company. The notification and offering circular were cleared, and the offering circular dated, on May 21, 1962.

II

The Commission has reasonable cause to believe that:

A. The terms and conditions of Regulation A have not been complied with in that:

1. The notification filed by the issuer omits to state a material fact in that the issuer fails to disclose, as required by Item 10 of Form 1-A, that American Trailer Rentals Company (hereinafter referred to as ATR), an affiliate of the issuer, is presently contemplating a public offering of securities as evidenced by the fact that said

affiliate had filed a registration statement with the Commission on December 11, 1961.

2. The offering circular omits to state material facts and contains a materially misleading presentation of facts and untrue statements of material facts in that:

a) it fails to disclose all direct and indirect interests of two directors of the issuer in the affiliate of the issuer;

20 b) it fails to state that the major portion, if not all, of the offering has been and is being made solely to ATR trailer owners in exchange for trailers;

c) it fails to disclose that the present offering and the contemplated offering are but two steps in an integrated plan of financing which will ultimately result in the reorganization and refinancing of ATR;

d) it fails to disclose that ATR trailer owners are merely being offered an opportunity to exchange their interest in ATR for stock in substantially the same enterprise;

e) it fails to disclose that the directors of ATR formed the issuer for the purpose(s) of:

(1) supplying the issuer with an attractive balance sheet to facilitate the sale of additional stock for cash;

(2) eliminating the financial burden on ATR caused by its contractual obligations under trailer management contracts;

(3) relieving the present officers and directors of ATR from potential liability under the Securities Act of 1933, as amended;

f) it fails to disclose accurately and adequately the nature of the trailer rental system through which the issuer will operate and makes false and misleading representation with respect thereto;

g) it fails to disclose that the trailers to be acquired (1) might be defective, (2) that such trailers were manufactured by a former affiliate of ATR, and (3)

that ATR's present management has never been able to operate its system at a profit.

B. The offering has been and is being made in violation of Section 17 of the Securities Act of 1933, as amended.

III

IT IS ORDERED, pursuant to Rule 261(a) of the General Rules and Regulations under the Securities Act of 1933, as amended, that the exemption under Regulation A be, and it hereby is, temporarily suspended.

21. NOTICE IS HEREBY GIVEN that any person having an interest in the matter may file with the Secretary of the Commission a written request for hearing within thirty days after the entry of this order; that within twenty days after receipt of such request the Commission will, or at any time upon its own motion may, set the matter down for hearing at a place to be designated by the Commission, for the purpose of determining whether this order of suspension should be vacated or made permanent, without prejudice, however, to the consideration and presentation of additional matters at the hearing; that, if no hearing is requested and none is ordered by the Commission, this order shall become permanent on the thirtieth day after its entry and shall remain in effect unless or until it is modified or vacated by the Commission; and that notice of the time and place for any hearing will promptly be given by the Commission.

By the Commission.

ORVAL L. DEBOIS
Secretary

Exhibit 4 to Motion**PROSPECTUS**

Securities and Exchange Commission

Received Jan. 15, 1963

Received Dec. 11, 1961

Chicago Regional Office

AMERICAN TRAILER RENTALS COMPANY

a Colorado corporation

\$4,000,000

Fleet Participation Contracts

\$2,000,000

Trailer Investment Contracts

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The Fleet Participation Contracts and the Trailer Investment Contracts provide for the operation and management of automobile type utility trailers by the Company in the rental of the trailers to the public for local use or one-way trips throughout the United States. The Company does not own the trailers but the trailer owner retains title to the trailers which are leased to the Company under the Contracts.

The Fleet Participation Contract provides that the trailer owners entering into this Contract with the Company will participate in 35% of the monthly gross rental income of the fleet of trailers operated by the Company pursuant to this contract after payment of fleet operational expenses, in the proportion of the contract cost of the Fleet Investment Contracts.

The Trailer Investment Contract provides that the trailer owner will be paid monthly 1½% of the cost of his Trailer Investment Contract; this amount is payable irrespective of the rental income produced by the trailers operated by the Company pursuant to this Contract.

Prior to the recovery of the cost of the Contracts, payments under the Contracts reflect a return of capital.

The Contracts offered are for the purpose of purchasing and leasing to the Company, under either the Fleet Participation or Trailer Investment Contracts, the following models of trailers:

Model	Contract Cost Per Trailer	Underwriting Discount or Commission	Purchase Price Per Trailer(1)	Proceeds to the Company(2)
3½' x 6' Luggage	\$ 370.00	\$ 74.00	\$ 240.50	\$ 55.50
4½' x 6' Open Cargo	483.00	96.60	313.95	72.45
5' x 8' Open Cargo	515.00	103.00	334.75	77.25
5' x 12' 4 Wheel Open	760.00	152.00	494.00	114.00
3' x 6' Van	510.00	102.00	331.50	76.50
5' x 8' Van	735.00	147.00	447.75	110.25
5' x 12' 4 Wheel Van	1,080.00	216.00	702.00	162.00
Totals				
Fleet Participation Contract	\$4,000,000	\$ 800,000.00	\$2,600,000	\$600,000.00
Trailer Investment Contract	2,000,000	400,000.00	1,300,000	300,000.00
	\$6,000,000	\$1,200,000.00	\$3,900,000	\$900,000.00

(1) Plus sales tax, if any, relating to the purchase of the trailers. The trailers are equipped with clamp-on bumper hitch, automatic brake lights, tar-paulin, or fiber glass or metal top.

(2) Before payment of expenses of the Company in connection with offering, estimated at \$40,000.

The offering is not underwritten. The Fleet Participation and Trailer Investment Contracts will be offered and sold directly through its officers, directors and salesmen employed by the Company. There is no assurance that any of the Contracts will be sold. The selling commissions will be as above stated except in those states where the offering may be made which impose by law or regulation a lesser selling commission.

The date of this prospectus is

American Trailer Rentals Company, hereinafter called the Company, has filed with the Securities and Exchange Commission a registration statement under the Securities Act of 1933 relating to the Fleet Participation Contracts and Trailer Investment Contracts offered by this prospectus. Reference is made to such registration statement and exhibits thereto for further information.

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24 AMERICAN TRAILER RENTALS COMPANY

1123 Delaware Street
Denver 4, Colorado

ORGANIZATION

American Trailer Rentals Company was incorporated in Colorado on September 18, 1958. It is engaged in the renting of automobile type utility trailers to the public. They are rented for local use or one-way trips, and may be used for various purposes ranging from trash hauling to transporting furniture and personal goods. The trailers are rented to the public through station operators, and the Company now has approximately 700 station operators scattered throughout the country. Approximately 5,866 trailers, all of which are individually owned by trailer owners are operated by the Company. The Company performs the services of securing station operators, the purchase of the trailers for the owners, and placing the trailer with one of the station operators for rental to the public; the Company receives from the station operators the gross rental fee derived from the rental of the trailers and then distributes the gross rental income to the trailer owners in accordance with their respective agreements with the Company, and to the station operators. It also performs the functions of servicing the trailers and providing for their maintenance and repair. The trailers are operated under the name "American Trailers".

INTRODUCTORY

The Fleet Participation Contracts and Trailer Investment Contracts are offered for the purpose of adding to the presently existing number of trailers which the Company operates. The model of trailer to be purchased is at the discretion of the trailer owner at the time of entering into the Contracts, and the cost of the Contract varies according to the actual cost of the model of trailer. Any number or model of trailers may be covered by the same Contract. It is the expectation of the Company, however, that both types of Contracts will be applied to the purchase of the trailers in the following numbers: 5,294 of the 3½' x 6' vans; 1,633 5' x 8' vans, 1,111 5' x 12' 4 wheel moving vans; and approximately 1,690 of the other models of trailers. If all such models are purchased under the Contracts, the investment of the public in the 3½' x 6' vans will be \$2,700,000, in the 5' x 8' vans \$1,200,000, in the 5' x 12' 4 wheel moving vans \$1,200,000, and in the other models of trailer at an average Contract cost of \$532 of approximately 900,000.

The addition to the number of trailers which the Company now operates is dependent upon the sale of the Fleet Participation Contracts and Trailer Investment Contracts offered by this prospectus. The business of the Company in the renting of the trailers to the public is contingent upon the Company's successfully competing with presently operated utility trailer systems, two of which are substantially larger than the anticipated size of the Company's fleet through the sale of the Contracts. The offering and sale of the Fleet Participation Contracts will be made directly by the Company through its officers, directors and salesmen, who will be directly employed by the Company. No assurance can be made that any or all of the Contracts offered will be sold. Approximately 65% of the amount derived by the Company through the offering and sale of the Contracts will be applied to the purchase of trailers as the Contracts are entered into by the Company with the trailer owners, and the trailers will be entered into service by the Company as they are received from the manufacturer. The Company has not made and does not intend to make any arrangement for the repayment of any money received by it from the sale of the Contracts. The trailers will be purchased from DeMar, Inc., of Alliance, Ne-

braska, with whom the Company has entered into an exclusive agreement for the manufacture of the trailers.

The Fleet Participation Contracts provide that the holders of these Contracts will be paid monthly 35% of the gross rental income of the fleet of trailers operated pursuant to this type of Contract after payment of expenses of maintenance of this group of trailers. The holders of the Fleet Participation Contracts will participate in this portion of the gross rental income of these trailers in the proportion which their cost of the Fleet Participation Contract bears as against the total sale price of the Fleet Participation Contracts sold by the Company. The Trailer Investment Contracts provide that the owners will receive 1½% per month of the cost of their Trailer Investment Contracts, and this is without regard to the rental income of the individual trailers or fleet of trailers operated by the Company under this type of Contract. The holders of the Fleet Participation Contracts and Trailer Investment Contracts do not participate in the management of the Company or in the election of Directors of the Company.

Between the period of January 1, 1959, to April 12, 1961, the Company entered into trailer rental agreements relating to approximately 5,866 trailers and the trailer rental agreements had a total value of \$3,587,439.02. None

25 of these trailer agreements were registered under the Securities Act of 1933. The Company may have a contingent liability with respect to a portion of these trailer rental agreements. Section 12 of the Securities Act provides for liabilities arising out of the sale of securities in violation of the registration provisions of the Act, and provides that any person who sells a security in violation of the Act shall be liable to any person purchasing such security from him in a suit to recover the consideration paid, with interest, less the amount of any income received thereon, upon tender of the security, or for damages if he no longer owns the security. The statute of limitations with respect to this civil liability is one year from the date of the sale of the security. As of September 30, 1961 any such contingent liability would not be in excess of \$2,400,000.00.

USE OF PROCEEDS

The offering of the Fleet Participation Contracts and Trailer Investment Contracts will be made directly by the Company through its officers, directors and employed sales-

men. There is no assurance that any or all of the Contracts will be sold. In the event that all of the Contracts are sold, the selling commission to officers, directors and salesmen will amount to \$1,200,000. The amount which will be applied to the purchase of trailers will be \$3,900,000. The proceeds to the Company are estimated at \$900,000.

The Company will purchase the trailers as the Contracts are entered into and as the proceeds become available to it for such purpose. The trailers are manufactured on order of the Company and the time for fabrication of the trailer and placing it for rental to the public varies from two to four months. Title to the trailer is not held by the Company but issued in the name of the trailer owner. Each trailer is marked with an identifying serial number in order that the ownership of the trailer may be determined at all times.

The model of trailer purchased is at the discretion of the Contract purchaser. The Company, however, will seek diversification in the models of trailers, and anticipates that approximately the following number of trailers may be purchased: 5,294 3½' x 6' vans; 1,633 5' x 8' 1,111 5' x 12' 4 wheel moving vans; the balance in approximately 1,692 of the other models of trailers, which estimate is based upon the average Contract cost of the other trailers of \$532. As the Contracts are entered into the Company will apply approximately 65% of the proceeds derived from the sale of the Contracts to the purchase of the trailers as follows:

Description and Type	Cost of Trailers
3½' x 6' Luggage Trailers	\$240.50
4½' x 6' Open Cargo Trailers	313.95
5' x 8' Open Cargo Trailers	334.75
5' x 12' 4 wheel Open Moving Trailers	494.00
3' x 6' Utility Vans	331.50
5' x 8' Utility Vans	477.75
5' x 12' 4 wheel Moving Vans	702.00

The agreement for the manufacture of the trailers is with DeMar, Inc., of Alliance, Nebraska. This agreement is dated November 17, 1960, and gives DeMar the exclusive right to manufacture trailers for the Company for a period of 5 years or until a total of 40,000 trailers has been made by DeMar, Inc. The agreement allows DeMar to make

adjustments in the cost of the models of the trailers, providing any adjustments shall maintain the cost of the trailers at a competitive level with other trailer manufacturers. Marvin Young, now Treasurer and Director of the Company, terminated his employment by DeMar, Inc. on October 5, 1961. W. N. Marks, President and controlling stockholder of DeMar, Inc., holds proxies on 141,250 shares of the common stock of the Company and his proxy provides that it may not be revoked until the indebtedness of the Company to DeMar is retired.

The net proceeds to the Company if all Contracts are sold are estimated at \$900,000. The Company presently intends to use such proceeds in the approximate amounts and in the following order:

Payment of expenses of offering, estimated at	\$ 40,000
Payment of initial trailer license and permit fees . . .	80,000
Cost of transportation of trailers to station operators for initial renting to the public	100,000
Cost of setting up approximately 800 additional rental stations	56,000
Cost of setting up zone management and field organization	50,000
Cost of providing a fund for redistribution of trailers	80,000
26 Cost of fund for replacement and repair	135,000
Cost of providing additional accounting system for additional trailers	28,000

Payment of obligations:

Bank	\$ 25,000
DeMar, Inc.	132,861
Trailer Owners	84,822
Working capital for administrative expenses, printing of station operator directories, rental agreements, agreements with station operators . . .	242,683
	88,317
	<hr/>
	\$900,000

BUSINESS OF THE COMPANY

The business of the Company is the providing of the management, operational services and accounting for the owners of utility trailers in the renting of the trailers to the public for either local use or one-way trips throughout the United

States. The Company does not own any trailers. It purchases the trailers for the owners, secures their licensing, and places the trailers with one of its station operators for rental to the public. The Company has entered into agreements with approximately 700 station operators in the principal cities of the Country. The units are initially entered into operational service by placing them with such station operator as the Company feels will provide most advantageous renting to the public. The station operators are for the most part gasoline filling station operators.

The rental charge is collected in advance by the station operator. The rental charge now in effect for local use varies from \$4.50 to \$10.00 a day, depending on the model of trailer. The rental charge for one-way trips is based on a system of zones established by the Company, and the charge depends on the distance between the dispatching station and receiving station and the model of the trailer. The charge makes allowance for travel time, with an overtime charge for the time in excess of the estimated travel time. The Company has divided the country into 42 zones. One-way rental charges vary from \$9.50 for a one-way trip within the same zone for the 3½' x 6' open trailer to a maximum of \$167.50 for a cross-country trip of the 5' x 12' van trailer.

The agreements between the Company and station operator provide that the station operator shall display all of the trailers coming to his station, and will hook up the trailers by means of the clamp-on bumper hitch which accompanies each trailer. The station operator executes all rental agreements for the renting of the trailers, collects the gross rental charges, and remits each week the gross rental charge which he may collect. The station operator also has the duty to the proper care and cleanliness of the trailer, including the minor maintenance work and tire repair. The Company pays monthly to the station operator a percentage of the gross rental charges which he has collected the preceding month. The station operator is paid 30% of the gross rental of trailers rented by him for one way trips and 40% of the gross rental of trailers received by him for local use.

The rental agreement for either local use or one-way trips provides that the renter shall be liable for all damage to or loss of the trailer, ordinary wear and tear excepted.

The trailers are of all-steel construction, and each bears an identifying serial number in order that its ownership by trailer owner may be determined. Each trailer is marked with the name "American Trailers"; and each trailer is equipped with a clamp-on bumper hitch and automatic brake lights; the open trailers are equipped with tarpaulin and the vans have either fiberglass or metal tops.

The Company contemplates the extension of its rental system by the addition of other station operators throughout the country and the hiring of zone managers whose duty it will be to secure additional station operators, provide for the maintenance and repair of the trailers beyond that done by the station operators, and to provide for even distribution of the trailers throughout its system.

In the renting of trailers, the Company will directly compete with 5 other trailer rental organizations who are now engaged in business on a national scale, as well as numerous other one-way organizations which operate systems in portions of the United States. Two of these national organizations are substantially larger than the system now operated by the Company.

The Company now has approximately 5,866 trailers in its system. These are operated by the Company pursuant to various trailer leasing agreements which provide for monthly payments to the trailer owners of amounts varying from 2 to 3%; trailer rental agreements relating to 161 trailers provide for payment to the trailer owners of 35% of the rental income derived by these trailers after payment of the expenses of repair and maintenance of these trailers.

SUMMARY OF OPERATIONS

The combined summary of earnings of American Trailer Rentals Company and affiliate has been examined by Alexander Grant & Company, independent certified public accountants, for the two years and nine months ended June 30, 1961. The auditors could not give an unqualified opinion on this statement, which should be read in conjunction with the combining balance sheets, notes, and the report of Alexander Grant & Company, included in this prospectus. There were no transactions effecting this statement by American Trailer Rentals Company since the date of incorporation (Note 1) to September 30, 1958 (end of the first fiscal year).

Year ended September 30, 1961

	Three months ended Sep- tember 30, 1961 (un- audited)	Nine months ended June 30, 1961 (a)	Year ended September 30 1960 (a)	Year ended September 30 1959 (a)
Trailer sales operations				
Sales	\$2,505,412	—	\$2,505,412	\$641,331
Less commissions paid	533,574	—	533,574	112,571
Net sales	1,971,838	—	1,971,838	528,760
Cost of trailers sold (d)	1,614,345	—	1,614,345	413,787
Gross profit on trailer sales	357,493	—	357,493	114,973
Trailer rental operations				
Gross rentals	303,137	\$130,743(b)	172,394	76,195
Payments to station operators	91,462	41,180	50,282	22,041
Payments to trailer owners(e)	422,617	122,657(e)	299,960(e)	157,145
	514,079	163,837	350,242	179,186
Gross loss from trailer rentals	210,942	33,094	177,848	102,991
Combined gross profit or (loss)	146,551	(33,094)	179,645	11,982
Operating expenses	359,083	99,989(f)	259,094(f)	120,924
Operating loss	212,532	133,083	79,449	108,942
Interest expense	16,668	4,532	12,136	16,594
Net loss before special items	229,200	137,615	91,585	125,536
Special items:				
Write off of accounts receivable from former affiliated com- panies	9,286	—	9,286	232,690
Par value of common stock issued for services—				
100,000 shares (100%) of Executive Sales Company \$.50 par value stock	—	—	—	50,000
	9,286	—	9,286	232,690
Net Loss	* 238,486	\$137,615	\$ 100,871	\$358,226
				\$200,121

(a) Examined by independent accountants.

(b) Rental revenue during the three months ended September 30, 1961, were adversely affected by having certain trailers recalled for conversion by the manufacturer. See note 17 of notes to financial statements.

(c) Payments to trailer owners for the nine months ended June 30, 1961 and the three months ended September 30, 1961, were reduced by approximately \$35,000 and \$60,000 respectively as a result of certain trailer owners agreeing to contract amendments. See note 6 of notes to financial statements.

(d) Costs of trailers on which there were delayed purchases have been allocated to the periods in which funds therefor were received. See note 5 of notes to financial statements.

(e) See note 5 of notes to financial statements for payments to trailer owners in excess of contract requirements.

(f) Operating expenses include charges for stock issued to a principal holder of equity securities in exchange for services as follows:

Nine months ended June 30, 1961 30,000 shares at \$.50 \$15,000

Three months ended September 30, 1961 30,000 shares at \$.50 \$15,000

(g) Unaudited amounts shown for the three month period ended September 30, 1961 have been adjusted to reflect a fair statement of operating results.

The Company actually did not begin operations until January, 1959. During the year 1959, 504 trailers were entered into the system. During the year 1960, the number of trailers was increased to 1,726. During the year 1961, the total number of trailers was increased to 5,866, with no new trailers entering the system after April 12, 1961, the date on which the Company ceased offering the trailer rental agreements. 161 trailers, having a total value of \$81,099.54 are operated under a trailer rental agreement which provides for payment to the trailer owner of 35% of the rental income of the individual trailers after payment of repair and maintenance. The remainder of the trailers are operated under trailer rental agreements which provide for a flat monthly payment to the trailer owners. 4,953 trailers, having a total value of \$3,057,933.96 are operated pursuant to a 2% trailer rental agreement. 2 trailers having a value of \$801.50 are operated pursuant to a 2.2% trailer rental agreement. 23 trailers having a total value of \$13,265.47 are operated pursuant to a 2.5% trailer rental agreement. 727 trailers, having a total value of \$434,338.55 are operated pursuant to a 3% trailer rental agreement. The Company's fixed obligation to these presently outstanding flat fee trailer rental agreements amounts to \$74,538.11 per month.

HISTORY OF THE COMPANY

The Company was incorporated on September 18, 1958, by David W. Adams (now deceased), Jack Gribble, and Richard J. Rutherford, who were the promoters of the Company. They also incorporated Executive Sales Company for the purpose of selling trailer rental agreements. There were also created, prior to April 12, 1961, separate state corporations for the sale of trailer rental agreements in the midwestern states. Executive Sales Company and the separate state corporations have since been merged into the Company, the Company issuing 110,000 shares of its 50¢ par value common stock in exchange for all the outstanding common stock of Executive Sales Company, and issuing 112,500 shares of its 50¢ par value common stock to the stockholders of the various state corporations. None of the promoters now has any connection with the Company, except that Mr. Rutherford presently holds 68,750 shares of

stock of the Company. During the period between January 1, 1959, and April 12, 1961, the Company entered into the various trailer rental agreements relating to the trailers which it now operates. None of the trailer rental agreements were registered under the Securities Act of 1933. The Company may have contingent liability with respect to a portion of the trailer rental agreements. Section 12 of the Securities Act provides for civil liabilities arising out of the sale of securities in violation of the Act, and provides that any person who sells a security in violation of the Act shall be liable to any person purchasing such security from him in a suit to recover the consideration paid, with interest, less the amount of any income received thereon, upon tender of the security, or for damages if he no longer owns the security. The statute of limitations with respect to this civil liability is one year from the date of the sale of the security. As of September 30, 1961, any such contingent liability would not be in excess of \$2,400,000.

As of September 30, 1961, 100 trailers manufactured prior to September 30, 1960, were unlocatable and were considered lost. In May, 1961, 659 trailers were discovered to be defective in design and unsuitable for rental. These defective trailers are currently being corrected by the trailer manufacturer at no expense to the Company. In June, 1961, it was also discovered that some trailers having substandard tires were being delivered. The Company has refused delivery since that date of trailers having substandard tires. The Company may have a cause of action against the trailer manufacturer for loss of rental income of the defective trailers. This amount of loss has not as yet been estimated, nor has the Company made any determination as yet to recover any loss of income from the manufacturer.

As of June 30, 1961, the Company was committed to the payment to trailer owners for the ensuing year ending June 30, 1962, in the amount of \$894,457.40. Trailer rental agreements for approximately 3,000 trailers were renegotiated with the trailer owners, and the owners of the trailers agreed to forego any payments under their rental agreements for a period of 6 months, with 6 months to be added to the 10-year term of their trailer rental agreements.

DESCRIPTION OF FLEET PARTICIPATION CONTRACTS AND TRAILER INVESTMENT CONTRACTS

The Fleet Participation Contracts and Trailer Investment Contracts are substantially the same, except with respect to the compensation to be paid to the trailer owners. Each provides that the owner shall retain title to the trailers, and that the Company will have the leasing of the trailers for a period of 10 years.

The Trailer Investment Contract provides that the trailer owner will be paid monthly 1½% of the cost of the Contract, the cost including the selling commission, the amount allocated for the purchase of the trailers, and the proceeds to the Company. The Company pays in connection with these Contracts all initial applicable license fees, taxes, or permits required by any state or government authority. Sales tax, if any, is paid by the trailer owner. The Company carries public liability and property damage insurance with respect to these trailers, but is a self-insuror as to the theft, damage or destruction of the trailers, and in event of damage trailers are repaired at Company expense and in the event of destruction or theft the Trailer Investment Contract terminates and the Company pays to the trailer owner the depreciated value of the trailer.

The Fleet Participation Contract provides for payment to all those holding the Fleet Participation Contracts of 35% of the gross rental income of this fleet of trailers, after payment of expenses of maintenance and repair of the trailers; the amount so paid is allocated among the participants according to the individual cost of the Contracts which cost includes underwriting commissions, cost of the trailers and amount allocated to the Company. In connection with these Contracts, all license fees, taxes or permits as may be required are paid from the gross income of this fleet of trailers. Public liability and property damage insurance at the rate of 38¢ per month per trailer is part of the operation cost, and as to these trailers the Company is a self-insuror as to theft, damage, or destruction. Damage repair is part of the operational cost of the trailers, but in the event of total destruction or theft the Company pays to the trailer owner the depreciated value of the trailer and the Fleet Participation Contract terminates.

30 Both Contracts have a term of 10 years, and provide that at the end of the 10-year period the trailer owner may take possession of the trailers or give to the Company the option to purchase the trailer for 10% of the original contract cost.

Before a trailer owner may determine his net taxable true income under these Contracts, he must deduct as a depreciation expense the percentage of the cost of his trailers each year from the money he receives from the Company. Such depreciation represents return of capital, and if in any year the net paid to the trailer owner is not in excess of the scheduled depreciation for that year there is no true income. There is no assurance that the net paid to a trailer owner in any year will equal the depreciation scheduled in that year under any of the following methods of depreciation, and therefore the original cost of the trailer may not be recovered in the time indicated under such methods.

The following methods of depreciation are available for use by the trailer owners:

1. The "Straight Line" method: One-sixth of the original cost is set aside each year by the owner as depreciation expense. This method provides for the recovery of the original cost of a trailer during the first six years of its life.
2. The "200% Declining Balance" method; Approximately 33 $\frac{1}{3}$ % is set aside the first year; 22.22% the second year; 14.81% the third year; 9.88% the fourth year; 6.58% the fifth year; 4.39% the sixth year; 2.90% the seventh year, etc. By this method, a greater part of the original cost is recovered during the first few years.
3. The "Sum of Years—Digits" method: Approximately 28.57% is set aside the first year, 23.81% the second year, 19.05% the third year, 14.29% the fourth year, 9.52% the fifth year, and 4.76% the sixth year. By this method a greater part of the original cost is recovered during the first few years, and the total cost is recovered in six years.

The amount set aside as depreciation and the disposition thereof is at the discretion of the trailer owner.

CAPITAL STRUCTURE

Title	Amount Authorized	Amount Outstanding	
		As of October 31, 1961	If all Securities being Registered are Sold
50¢ Par Value Common Stock (authorized 600,000 shares) . . .	\$ 300,000	\$ 219,000	\$ 219,000
Promissory Notes:			
Payable to officers, directors and stockholders . . .	179,424	179,424	179,424
Bank	25,000	25,000	25,000
De-Mar, Inc.	132,861	132,861	132,861
Trailer Rental Agreements			
35% of Gross Rental	81,099.54	81,099.54	81,099.54
3% of Trailer Cost	434,338.55	434,338.55	434,338.55
2½% of Trailer Cost	13,265.47	13,265.47	13,265.47
2% of Trailer Cost	3,057,933.96	3,057,933.96	3,057,933.96
Trailer Investment Contracts . . .	\$4,000,000	none	\$4,000,000
Fleet Participation Contracts . . .	\$2,000,000	none	\$2,000,000

As to the notes due officers, directors, and stockholders the principal amount of \$81,777.06 is subject to subordination agreements of the note holders that payments of principal and interest thereon shall be subordinated to payment of lease obligations to present and future trailer owners and that no amount shall be paid in the event any amount is due trailer owners. The \$90,000 of this amount was loaned the Company by James H. Daly, President of the Company, in September and October, 1961.

The Company has granted options to purchase its common shares, 50,000 shares for an indeterminate time at \$1.00 a share and 89,500 shares exercisable prior to August 1, 1966 at \$.50 a share.

OFFICERS AND DIRECTORS

The Company has the following officers and directors:

President and Director	James H. Daly Gillette, Wyoming
Executive Vice President and Director	I. H. Peters Alliance, Nebraska
Secretary and Director	Clark Hammond Burlington, Colorado
Treasurer and Director	Marvin Young Alliance, Nebraska
Director	Dr. James W. Monsour 1765 Sherman Street Denver, Colorado
Director	Ervin O. Mueller Ellendale, North Dakota
Director	Vincent Bagan Miles City, Montana
Director	Robert Jones Goodland, Kansas
Director	Clayton Johnson Dickinson, North Dakota

Mr. Daly has been engaged in ranching in the area of Gillette, Wyoming, for the past 30 years. He also is the owner of an automobile sales agency in Denver. He became President of the Company in July, 1960.

Mr. Peters has been in the general contracting business at Alliance, Nebraska, for the past six years; this business is conducted under the name of I. H. Peters Company, of which he is the President and controlling stockholder. He was also President of the Nebraska Trailer Rentals Company and Vice President of the Iowa Trailer Rentals Company. He has been the Executive Vice President of the Company since July, 1960.

Mr. Hammon has been engaged in the real estate and insurance business at Burlington, Colorado, since 1949, in partnership with his brother, Charles C. Hammond. He

was Secretary-Treasurer of Colorado Trailer Rentals Company and Kansas Trailer Rentals Company. He has been on the Board of Directors of the Company since February, 1959.

Mr. Young is an accountant and was employed by DeMar, Inc., of Alliance, Nebraska, for a year ending October 15, 1961. Prior to that time he was employed by the United States government.

The Executive Committee of the Company is composed of Mr. Peters, Dr. Monsour, and Mr. Young.

Dr. Monsour has been engaged in the practice of medicine and surgery in Denver since 1956. He has been on the Board of Directors of the Company and Executive Committee since August, 1961.

David W. Adams (now deceased), Jack Gribble and R. J. Rutherford may be regarded as promoters of the Company. Mr. Gribble's connection with the Company was severed in February, 1959. Mr. Rutherford has had no participation in the management of the Company since July, 1960, but holds 68,750 shares of the 50¢ par value common stock of the Company on which proxies for 65,006 shares are held by W. N. Marks, President of DeMar, Inc., which proxy provides that it shall not be revocable until such time as the present indebtedness of the Company to DeMar, Inc., is paid. With the exception of Mr. Peters and Mr. Young, none of the officers and directors is paid a salary by the Company. Mr. Peters' remuneration is \$200 a week, and Mr. Young is paid \$850 a month.

PRINCIPAL SECURITY HOLDERS

The following persons held as of October 31, 1961, both beneficially and of record, more than 10% of the shares of stock of the Company:

Name and Address	Title of Class	Amount Owned	Type of Ownership	Percentage of Class
James H. Daly Gillette, Wyoming	Common	101,250	Record and Beneficial	23.1%
I. H. Peters Alliance, Nebr.	Common	22,500	Record and Beneficial	5.1%
Clark E. Hammond Burlington, Colo.	Common	8,920	Record and Beneficial	2.0%
Dr. James W. Monsour 1765 Sherman St. Denver, Colorado	Common	45,000	Record and Beneficial	10.2%
Ervin O. Mueller Ellendale, N. Dak.	Common	6,833 $\frac{1}{3}$	Record and Beneficial	.14%
Vincent J. Bagan Miles City, Mont.	Common	12,500	Record and Beneficial	2.8%
Robert Jones Goodland, Kansas	Common	4,108	Record and Beneficial	.9%
R. J. Rutherford 6808 E. 19th Ave. Denver, Colorado	Common	68,750	Record and Beneficial	15.6%
All directors and officers as a group:	Common	201,111 $\frac{1}{3}$	Record and Beneficial	45.3%

In addition, the above persons hold options to purchase shares of stock as follows: Mr. Daly 30,000; Mr. Peters, 15,000; Mr. Hammond, 5,710; Mr. Jones, 1,429. These options provide that these persons may purchase the shares of stock of the Company at 50¢ per share and expire August 1, 1966. DeMar, Inc., has the option for an indeterminate time to purchase 50,000 shares at \$1.00 a share. Hammond Brothers, a partnership composed of Clark E. Hammond and his brother, Charles C. Hammond hold an option expiring August 1, 1966 to purchase 45,000 shares at 50¢ per share.

PLAN OF DISTRIBUTION

The Company has not entered into an underwriting agreement with reference to the Fleet Participation Contracts and Trailer Investment Contracts offered by this prospectus. The Contracts will be offered and sold directly by the Company through its officers and through salesmen employed by the Company.

The selling commission for the sale of the Contracts is 20% of the face amount of the Contract, and if all of the

Contracts are sold the full commission will amount to \$1,200,000. The selling commission will be reduced in those states which by law or regulation impose a lesser selling commission.

MATERIAL LITIGATION

There are no legal proceedings to which the Company is a part nor is any contemplated or threatened. The Company may have a cause of action against DeMar, Inc., for the loss of income because of the defective manufacture of 659 trailers, which were manufactured with defective axles, as well as loss of income relating to trailers having defective tires, as well as cost of replacement of the tires. The amount of loss occasioned by the company has not been determined, nor has the Company made any determination to institute legal proceedings against DeMar, Inc.

LEGAL OPINIONS

Legal matters in connection with the Fleet Participation Contracts and Trailer Investment Contracts have been passed upon for the Company by Arthur W. Burke, attorney at law, American National Bank Building, Denver, Colorado, and Gilbert C. Maxwell, attorney at Law, First National Bank Building, Denver, Colorado.

The financial statements included in this prospectus and the related schedules omitted from this prospectus but included in the registration statement have been included in reliance upon the opinions of Alexander Grant and Company, independent certified public accountants, to the extent set forth in such opinions contained herein, and in the registration statement, and upon their authority as experts in the giving of such opinions. It should be noted that Alexander Grant and Company could not express an overall opinion as to the statement of operations.

AUDITORS' REPORT**Board of Directors****American Trailer Rentals Company**

We have examined the combined balance sheet of AMERICAN TRAILER RENTALS COMPANY and affiliate (both Colorado corporations) as of June 30, 1961, and the related combined statement of operations for the two years and nine months ended June 30, 1961. Our examination included such tests of the accounting records and such other auditing procedures which were practicable and which we considered necessary in the circumstances.

Satisfactory evidential matter was available for our examination to support trailer purchases during all periods under review. However, the present management of the companies was unable to present for our examination documents, other than cancelled checks, supporting disbursements for a significant portion of the expenses. Since the inception of the companies, internal controls were limited and the accounting records were not maintained on a basis to readily provide financial statements in accordance with generally accepted accounting principles. Accordingly it was necessary for us to recommend significant adjustments to the accounts for all periods under review. The present management is taking action to correct this situation.

In our opinion, the accompanying combined balance sheet presents fairly the financial positions of American Trailer Rentals Company and affiliate at June 30, 1961, in conformity with generally accepted accounting principles.

Because of the absence of evidential matter to support expense disbursements and the materiality of adjustments to the operating accounts for the periods under review, we are precluded from expressing an overall opinion as to the combined statement of operations. It is our opinion, however, that the trailer sales, cost of trailer sales, and commissions on trailer sales are presented fairly, in conformity with generally accepted accounting principles.

ALEXANDER GRANT & COMPANY
Certified Public Accountants

Denver, Colorado
September 10, 1961

American Trailer Rentals Company and Affiliate

COMBINED BALANCE SHEETS

ASSETS	June 30, 1961 (Examined by independent accountants)	September 30, 1961 (unaudited)
CURRENT ASSETS		
Cash	\$ 1,088	\$ 25,597
Notes and accounts receivable		
Trailer rentals	8,337	16,556
Other	15,295	10,027
Prepaid expenses	2,021	1,806
Total current assets	\$ 26,741	\$ 53,986
FIXED ASSETS—AT COST (Note 2)		
Furniture, fixtures and leasehold improvements	\$ 32,444	\$ 35,756
Less accumulated depreciation and amortization	7,489	8,266
	\$ 24,955	\$ 27,490
OTHER ASSETS		
Deferred cost of establishing rental station, less amortization (Note 3)	27,000	25,313
Sundry	347	1,698
	\$ 27,347	\$ 27,011
	\$ 78,043	\$108,487

The accompanying notes are an integral part of these statements.

American Trailer Rentals Company and Affiliate
COMBINED BALANCE SHEETS

LIABILITIES	June 30, 1961 (Examined by independent accountants)	September 30, 1961 (audited)
CURRENT LIABILITIES		
Notes payable		
Bank (guaranteed by officers)	\$ 25,000	\$ 25,000
Officers, directors, and stockholders (Note 4)	89,237	139,424
Other	14,689	14,642
Accounts payable		
Trade	36,721	48,166
Delayed trailer purchases (Note 5)	26,104	18,500
Station operators	13,402	15,634
Trailer owners (Note 6)	9,376	84,822
Liability on lost trailers (Note 7)	35,000	35,000
Payables to De-Mar, Inc. (Note 5)		
Notes	132,862	132,861
Accounts	246,717	96,233
Less funds held in escrow for payments on trailers	\$379,579	\$229,094
Accrued liabilities	\$158,031	\$ 1,804
Total current liabilities	\$221,548	\$227,290
	10,303	16,604
	\$481,380	\$625,682
OTHER LIABILITIES		
Deposits on franchises (Note 13)	105,631	12,500
Sundry payables (liquidated through issuance of common stock) (Note 13)	25,000	—
Equipment lease contract (Less \$772 current maturities)	—	3,438
CONTINGENCIES AND COMMITMENTS		
(Notes 9, 10, 11, and 12)	—	—
DEFICIT IN STOCKHOLDERS' EQUITY		
Contributed capital		
Common stock (Notes 13 and 14)	117,750	214,000
Additional contributed capital (Note 15)	10,500	52,300
Deficit in retained earnings (Note 16)	(659,218)	(796,833)
Less common stock reacquired and held in treasury—at cost	(530,968)	(530,533)
	2,000	2,000
	(532,968)	(532,533)
	\$ 79,043	\$108,487

The accompanying notes are an integral part of these statements.

36 AMERICAN TRAILER RENTALS COMPANY AND AFFILIATE
Notes to Combined Financial Statements
June 30, 1961 (examined by independent accountants)
September 30, 1961 (unaudited)

1—BASIS OF COMBINATION

The combined financial statements include the accounts of American Trailer Rentals Company (hereinafter referred to as the Company) and Executive Sales Company since the dates of their incorporation (September 18, 1958 and October 17, 1958 respectively); however, the Company had no operations between September 18, 1958 and September 30, 1958 (the close of its first fiscal year). The Company and Executive Sales Company were operated under common management and control, and though various individuals hold stock in both corporations, there is no parent-subsidiary relationship involved. Intercompany accounts have been eliminated from the combined totals.

It is planned that Executive Sales Company will be merged into the Company, subsequent to September 30, 1961, by an exchange of 110,000 shares of the common stock of the Company for all the outstanding common stock of Executive Sales Company. When this merger is consummated, the accounts of the two corporations will be combined on the basis of a "pooling-of-interests".

2—FIXED ASSETS

Fixed assets are depreciated over their estimated useful lives on the "straight-line" basis. Estimated lives of assets used for determining depreciation rates are as follows:

Leasehold improvements	... Life of lease
Automotive equipment 4 years
Furniture and fixtures 10-15 years
Office equipment 10-15 years

Expenditures for maintenance and repairs are charged to expense as incurred. The companies have had no renewals or betterments. Cost of assets sold or retired and the related amounts of accumulated depreciation are eliminated from the accounts in the year of sale or retirements,

and the resulting gain or loss is reflected in the statement of operations.

3—DEFERRED COST OF ESTABLISHING RENTAL STATIONS

Salaries, travel expenses, supplies, postage and other expenses of fieldman in the amount of \$33,750.00 have been capitalized as deferred costs of establishing rental stations. These costs are being amortized over five years from June 30, 1960. As of June 30, 1961, amortization of \$6,750.00 has been recorded. Additional amortization of \$1,687.50 was recorded in the three month period ended September 30, 1961.

4—NOTES PAYABLE TO OFFICERS, DIRECTORS, AND STOCKHOLDERS

As of June 30, 1961, certain officers, directors, and stockholders had signed subordination agreements pertaining to amounts due them on corporate notes totaling \$53,641.06 plus accumulated interest. The agreements state that the payments on the notes and of the accumulated interest thereon shall be subordinated to the payment of lease obligations to present and future trailer owners under trailer rental agreements and that no amount shall be paid on said notes in the event any amount is due any of said trailer owners. No additional subordination agreements were signed during the three months ended September 30, 1961, but subsequent to September 30, 1961 additional subordination agreements in the amount of \$28,130 were signed.

In September, 1961 an officer and stockholder loaned the Company \$50,000. This same individual loaned an additional \$40,000 to the Company in October, 1961.

All loans made to the corporations by officers, directors, and stockholders have been on an unsecured basis.

5—DELAYED TRAILER PURCHASES

Prior to November, 1960, certain amounts received for trailers were not expended to purchase trailers. In an agreement dated November 17, 1960, De-Mar, Inc. agreed to manufacture all but 57 of these trailers at a cost of approximately \$220,000. In September, 1961, De-Mar, Inc. accepted an order for an additional seventeen trailers.

On or about October 4, 1961, Executive Sales Company consummated a purchase agreement with another manufacturer for the residual forty trailers. Funds were placed in escrow on or about October 12, 1961, to cover the purchase price of these forty trailers.

37 As previously noted, certain amounts were received from investors for trailers but were not expended to purchase such trailers. Monthly remittances have been made to individual investors under the contracts covering these trailers even though the trailers had not been purchased and placed in the system. In addition, payments have been made to investors in certain "35% of gross income" contracts without relation to actual gross trailer rentals. Payments to these investors have exceeded the 35% of actual rental receipts from such trailers.

6—ACCOUNTS PAYABLE—TRAILER OWNERS

Accounts payable to trailer owners at June 30, 1961 were \$9,376. At September 30, 1961, the total amount payable to trailer owners had increased to \$84,822.

Certain trailer rental contracts were renegotiated with the trailer owners. Amounts due under such contracts were forgiven in consideration of the extension of the contract expiration dates. Had these contracts not been renegotiated, the accounts payable to trailer owners would have been approximately \$35,000 greater at June 30, 1961 and \$95,000 greater as of September 30, 1961.

7—LIABILITY ON LOST TRAILERS

The terms of the trailer rental contracts require the Company to maintain insurance adequate to compensate the trailer owners in the event of theft, damage or destruction of trailers. The Company has terminated all of its insurance policies for the above coverages and any loss of this nature will be borne by the Company. No definite plan for funding such losses has been initiated. As of June 30, 1961, one hundred trailers were unlocated and presumed lost. The amount of \$35,000 has been recorded at June 30, 1961, to cover the liability in connection with these lost trailers. There would have been no material change in the liability at September 30, 1961.

8—INCOME TAXES

Income tax returns have not been filed for either corporation since dates of incorporation. No income tax liability is estimated on such returns. Arrangements are being made for the preparation and filing of the necessary tax returns.

9—CONTINGENT LIABILITIES

The trailer rental contracts, which the Company has entered into with owners of trailers since September, 1958, have been registered under the Securities Act of 1933. The staff of the Securities and Exchange Commission in April, 1961, stated that these contracts may have been offered and entered into in violation of the Securities Act of 1933. Under the Securities Act of 1933, a person who entered into such contracts from the Company, in the event they should have been registered under such Act, can within a year recover the consideration paid for such trailer rental contract with interest thereon, less the amount of income received thereon, or for damages if he no longer owns the contract. The contingent liability of the Company attaching to the contracts entered into during the twelve month period prior to June 30, 1961, would not be in excess of \$2,643,000. At September 30, 1961, this contingent liability would not be in excess of \$2,400,000.

10—COMMITMENTS

The Company is committed on present rental contracts to pay to trailer owners approximately \$785,000 during the next twelve months. If certain trailer owners had not agreed to amend and postpone payments, the Company's commitment under the contracts would have been approximately \$895,000 for the next twelve months.

11—LONG-TERM LEASE

The Company executed a lease during March, 1959, providing for the rental of the office building in which it maintains its executive offices. This lease expires on March 31, 1969, and provides for annual rentals of \$7,200.00.

12—AGREEMENT WITH DE-MAR, INC.

On November 17, 1960, an agreement was entered into with De-Mar, Inc. wherein De-Mar, Inc. was granted the exclusive right to manufacture trailers for a period of 5 years or for 40,000 trailers, whichever occurs first. The price of trailers to be manufactured is to be maintained at a competitive level with other established trailer manufacturers, cash being forwarded as the trailers are ordered.

13—COMMON STOCK

On June 12, 1961, the shareholders and directors of the Company approved a change in the authorized common stock wherein the authorized shares were increased from 200,000 shares to 600,000 shares of \$.50 par value. The amendment for such change was filed with the Secretary of State of Colorado on July 11, 1961.

During August, 1961, the Company issued 152,500 shares of its common stock in payment of certain liabilities for deposits on franchises and services. The total amount of the liabilities paid in this manner was \$118,050. On September 1, 1961, the Company issued 30,000 shares of its common stock to an officer and stockholder in consideration of certain loans made to the Company by him.

The following schedule sets forth the details of the common stock account:

	Common Stock, par value \$.50 per share			
	Authorized	Issued	Treasury shares	Outstanding shares
June 30, 1961 (examined by independent accountants)				
American Trailer Rentals Company	200,000	135,500	2,500	133,000
Executive Sales Company	100,000	100,000	—	100,000
Total	300,000	235,500	2,500	233,000
September 30, 1961 (Unaudited)				
American Trailer Rentals Company	600,000	328,000	2,500	325,500
Executive Sales Company	100,000	100,000	—	100,000
Total	700,000	428,000	2,500	425,500

After the exchange of Executive Sales Company common stock for 110,000 shares of common stock of American Trailer Rentals Company, subsequent to September 30, 1961, the deficit in stockholders' equity would appear as follows on a pro-forma basis:

Common stock, par value \$.50

Authorized	600,000 shares	\$300,000
Issued	<u>438,000</u> shares	<u>219,000</u>
Additional contributed capital		47,300
Deficit in retained earnings		(796,833)
		<u>(530,533)</u>
Less common stock reacquired and held in treasury—at cost		2,000
Deficit in stockholders' equity		<u><u>\$(532,533)</u></u>

14—Stock Options

At a special meeting on June 12, 1961, the Board of Directors granted certain options to purchase common stock of the Company and ratified and confirmed the previous granting of other options. At June 30, 1961, there were 139,500 shares of the company's common stock reserved for such purpose with 50,000 shares exercisable for an indeterminate time at \$1.00 per share and 89,500 shares exercisable within five years at \$.50 per share. Using book value as the fair value for this purpose, fair value at the dates the options were granted was zero.

The Company intends to credit the common stock account with the par value of stock sold and the excess, where applicable, of proceeds over the par value of the stock will be credited to additional contributed capital.

There was no change in the outstanding options during the three months ended September 30, 1961.

15—ADDITIONAL CONTRIBUTED CAPITAL

The additional contributed capital consist of the following:

Excess of proceeds over par value of common stock sold prior to June 30, 1961	\$10,500
Excess of proceeds over par value of common stock issued in August and September, 1961	41,800
Additional contributed capital—September 30, 1961	52,300

39 16—DEFICIT IN RETAINED EARNINGS

A reconciliation of the combined deficit in retained earnings follows:

Year ended September 30, 1961					
	Three months ended September 30, 1961	Nine months ended June 30, 1961*		Year ended, September 30, 1960* 1959*	
Total (un- audited)	(un- audited)				
Deficit in retained earnings—					
beginning of period	\$558,347	\$659,218	\$558,347	\$200,121	\$ —
Loss for period	288,786	137,615	100,871	358,226	200,121
Deficit in retained earnings—					
end of period	\$796,833	\$796,833	\$659,218	\$558,347	\$200,121

* Examined by independent accountants.

17—DEFECTIVE TRAILERS

During May, 1961, 659 trailers were discovered to be defective in design and unsuitable for rental. Corrective measures are currently being made by the trailer manufacturer at no expense to the company. The loss of income during the period of inactivity on these trailers cannot be reasonably estimated. As of September 30, 1961, conversions correcting the above deficiency had been completed on approximately 50% of these trailers.

18—EXTRA-ORDINARY FUTURE TIRE REPLACEMENT COSTS

During June, 1961, it was discovered that trailers having substandard tires were being delivered. Delivery of trailers is currently being refused on trailers having this type of

tire. The number of trailers with substandard tires which have been accepted into the rental system is not known. The extent of the future liability, if any, of the Company or the trailer manufacturer that may result from excessive tire replacement costs can not reasonably be computed at this time.

19—SUPPLEMENTARY PROFIT AND LOSS INFORMATION

The items shown hereunder were charged directly to profit and loss as operating expenses. There were no charges to other accounts for these items.

Year ended September 30, 1961

	Three months ended September 30, 1961 Total (un- audited)	Nine months ended June 30, 1961*	Year ended September 30, 1960*	Year ended September 30, 1959*
Maintenance and repairs ..	\$ 137	\$ 73	\$ 64	\$ 206
Depreciation and amortiza- tion of fixed assets	3,946	776	3,170	7,515
Amortization of intangible assets				3,449
Deferred cost of estab- lishing rental stations	6,750	1,687	5,063	1,687
Organization expense	66	.17	49	66
Taxes				
Payroll	2,392	593	1,799	991
Other	573	130	443	253
Rent	7,251	1,800	5,451	5,527

* Examined by independent accountants.

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(File endorsement omitted)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In Proceedings for an Arrangement No. 33276

In the Matter of
AMERICAN TRAILER RENTALS COMPANY, Debtor.

Order of Reference to Referee Benjamin C. Hilliard, Jr.
as Special Master—February 26, 1963

At Denver, in said District, on the 26th day of February, 1963.

The Securities and Exchange Commission having filed a motion to dismiss the said proceeding and a motion to stay

a hearing scheduled for March 1, 1963 upon issues relating to the confirmation of the Debtor's proposed arrangement pending the determination of the motion to dismiss, the Court finds that all of proceedings in the matter have heretofore been heard by the Honorable Benjamin C. Hilliard, Jr., as Referee in Bankruptcy and that the said motions should be referred to the said Referee in Bankruptcy as Special Master to hear and report thereon.

IT IS THEREFORE ORDERED that the motions of the Securities and Exchange Commission to dismiss the proceeding and to stay the hearing on confirmation be and are hereby referred to Referee Benjamin C. Hilliard, Jr., as Special Master, to hear and report thereon.

ALFRED A. ARRAB

United States District Judge

56

(Filed April 17, 1963)

(Filed March 15, 1963)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

Bankruptcy Case No. 33276

In the Matter of
AMERICAN TRAILER RENTALS Co., *Debtor.*

Transcript of Proceedings—February 26, 1963

Appearances:MR. GILBERT C. MAXWELL and
MR. ARTHUR W. BURKS, JR.*Attorneys at Law*
For the Debtor.MR. WILLIAM D. SCHEID and
MR. WILLIAM J. COONEY*Attorneys at Law*
For the Securities and Exchange Commission.

Proceedings had before the HONORABLE BENJAMIN C. HILLIARD, Jr., Chief Referee in Bankruptcy, in the United States District Court, District of Colorado, on the 26th day of February, 1963 at Denver, Colorado.

(THEREUPON, the following proceedings were had:)

57 **Colloquy Between the Referee and Counsel**

The Referee: This is a continued "first meeting" of the American Trailer Rentals Company.

Mr. Gilbert Maxwell, attorney for the debtor company has appeared; Ivan H. Peters, executive vice president of the debtor company is also present; and Mr. William D. Scheid, an associate of the Securities and Exchange Commission is present.

Are there any other counsels desiring to enter an appearance?

Mr. Phipps: Allen Phipps. I represent Alexander Grant and Co. a firm of accountants. If I may make a statement of our client's view of this thing?

The Referee: Very well.

Mr. Phipps: We are perfectly willing to go along with this arrangement so long as Alexander Grant and Co.'s recourse against the guarantors of the note from American Trailers is not prejudiced.

The Referee: I presume it is a matter of judgment on the part of counsel for Alexander Grant and Co. that anything binding on the guarantor—this Court has jurisdiction?

Mr. Phipps: I cannot answer that exactly. I would like perhaps, to confer with counsel to see if we could work it out—but we still have the guaranteed position which we would like not to have prejudiced.

58 The Referee: I do not think we need to discuss that at this particular moment.

Are there any other counsels who desire to enter their appearances?

Mr. Stanfield: F. W. A. Stanfield. I represent a group of small investors—three Chinese and two non-Chinese, if you will.

The Referee: What is your address, sir?

Mr. Stanfield: Box 667, Eloy, Arizona.

The Referee: We have a rule in this jurisdiction that if you are going to participate beyond the attendance of the meeting itself and examination of witnesses, that you must be associated with a local counsel but we will permit you to appear today.

Mr. Carroll: John Carroll, appearing for Charles L. Hanaban of Cheyenne Wells. My address is 516 Denver U.S. National Bank Center.

The Referee: Are there any persons present who desire to examine Mr. Peters further? He was examined initially—at the initial session of this meeting.

Are there any other witnesses to be adduced on the part of the debtor, Mr. Maxwell?

Mr. Maxwell: I would like to ask Mr. Phipps—
59 I am not aware that a proof of claim has been filed.

Mr. Phipps: I believe it has.

Mr. Maxwell: If it is filed, we would like to add it into the total. Actually we did not get a chance to count.

The Referee: Very well. In procedural matter, the Securities and Exchange Commission has appeared in the matter and filed a motion under Section 328 for an application that this proceeding under Chapter XI be discontinued and dismissed and the matter converted into a Chapter X proceeding.

(Whereupon, there was a discussion off-the-record after which the following further proceedings were had:)

The Referee: If we are to proceed under Section 328, we will be obliged to apply to the Judge, either to himself here or refer it to a special master. I am not going to decline to receive a special master if a Judge chooses to make such a reference.

(Whereupon, there was a discussion off-the-record after which the following further proceedings were had:)

The Referee: The next order of business is the report of the committee which was appointed by the Court for the purpose of counting the claims and the amount—number of claims and the other procedures necessary to determine whether approval of the arrangement has been made by the creditors.

What progress has the committee made, gentlemen?

Mr. Andrew: I have been appointed as the spokesman for the committee, your honor.

We had hoped to have a written report but circumstances prevented it due to the continuing influx of claims. As a consequence, we have now totaled claims filed up to and including February 21st; there have been additional claims filed since then.

At the present, we have in round figures as of February 21, 1963, 525 claims filed. I might note at this time that not all of these claims are necessarily valid—some lack signatures, some lack amounts. But documents purporting to be claims in the number of 525 was filed as of February 21st.

As of February 21st there were also 354 acceptances filed which come from those 525 claims.

The Referee: How many acceptances?

Mr. Andrew: 354. We would not care to be held to this figure but we total it at \$486,898.64 as of February 21st; total acceptances \$238,584 which is slightly less than the majority in dollar amount.

We would also note that there were additional—approximately 115 acceptances filed over and above the 354 which I mentioned which were not accompanied by a claim form—people were filing acceptances without filing a claim. Acting on your preliminary instructions at the last meeting we simply made a note of those acceptances but did not include it in our totals.

There is not a sufficient dollar majority to accept the plan and the committee has agreed that this should not be the final report of the committee since we would still have to tabulate these and in addition, we believe you should now give a cut-off date and from that date, we may reach a definite final total.

The Referee: It seems to present an impossibility in that regard. I do not find a provision of a cut-off date so long as the meeting is in session and that order of business is still before the meeting the right to file a claim is continued. What are we going to do about that, Mr. Andrew?

Mr. Andrew: It would seem to me, the meeting itself should be continued allowing us one more chance at recapitulating or totalling the claims and at that point we could count the claims and the meeting could be closed. I don't see no other way.

The Referee: I wonder if it is possible, during the course of the day to do that?

62 Mr. Andrew: We could do that— However, Mr. Maxwell has one or two large creditors whose claims are apparently defective. I think it appears if those claims are righted, the plan—

The Referee: I think Mr. Maxwell has a personal matter this afternoon.

Mr. Burks: We also have a matter, your honor, of a claim filed by De-Mar, Inc. of Alliance, Nebraska which I had mentioned previously and if the claim from De-Mar, Inc. were to anyway affect the acceptance of the plan, I would file an objection to the claim as not being a proper valid claim although in proper form.

The Referee: As I understand, you have counted that?

Mr. Burks: Yes, sir; \$99,000. And they did not accept and we claim they have no claim.

The Referee: In fixing a cut-off date for claims filed, shall we say up to the close of business today will be accounted and then we will recess this meeting. Do you have any views on that, Mr. Maxwell?

Mr. Maxwell: Yes, sir. One claim which I am concerned with is that by James Daly who is the president of the company. His claim is back except as to his signature

and as to name; total of \$201,000 and this is actual
63 money that he put into the company. He lives in Gillette, Wyoming and to cut him off from participation would hardly be fair to him in view of the amount of money he has put into the company and the time he has given. Also, as Mr. Andrew says, the 115 other people who apparently filed acceptances without proof, I think consideration should be given to them.

The Referee: What is the committee's suggestion? As I understand, they want a cut-off date. Are you resisting that?

Mr. Maxwell: I did not anticipate it would be today. I anticipated that we would have sufficient time to give these people the right to participate as they have so indicated.

Also, I am not quite sure on this confirmation whether that would be the time for a cut-off date or whether the people can be given time after that to come in.

The Referee: Section 336 which deals with first meetings in these matters provides it must be done at the meeting and then when the meeting is adjourned that day, then confirmation is in order providing there has been acceptances.

Mr. Maxwell: I would like time to write to these people and send them proofs properly filled in for
64 them in advance and let them sign it. I should like at least sufficient length of time for the preparation of that letter and the return of it.

The Referee: So far as officers and the company itself are concerned, I am not impressed with the argument that they need more time.

Mr. Maxwell: I agree and I was amazed when the dollar amount was not shown. All we want is reasonable time in which to write to these people.

The Referee: Mr. Burks, I will ask you to go up to Mr. DeLaney's office and get my book.

Mr. Andrew: While he is gone, I would like to mention that the position of Mr. Englehardt and myself was that the power of attorney in acceptance did not give Mr. Peters the right to sign unsigned claims and fill in blank claims.

The Referee: As I recall, the power of attorney entitled him to vote the claims—

Mr. Maxwell: It never entitled him to sign the acceptances.

Mr. Andrew: It won't come to a head unless a cut-off date is assigned.

The Referee: Mr. Stanfield, I am afraid we are not helpful to you.

Mr. Stanfield: I'm afraid its all too clear, sir.

65 Mr. Scheid: Judge Arraj states he would like to refer the matter to you. I stated that I would present an order to him at the first available opportunity today if you are willing to proceed.

The Referee: I have sent for my hearing calendar for this reason, Mr. Scheid. The committee needs additional time to complete its duties; Mr. Maxwell wants some additional time because he feels he can get some additional acceptances.

So, it is clear now that we cannot continue this meeting today. That is going to leave this morning available for argument on your motion. Mr. Maxwell, for overwhelming personal reasons cannot be here today.

If that is agreeable, Mr. Scheid, we will proceed along that line that we can get the order ready for Judge Arraj.

Mr. Scheid: In connection with the motion, your honor, we do have a motion to stay the hearing set for March 1st.

The Referee: It is clear now that we are going to have to continue that anyhow.

Mr. Scheid: I was wondering about what date would be set to have the hearing on confirmation—whether there would be time for your honor's report and time to object to that report and a time for a hearing before 66 the Judge if need be.

The Referee: I am trying to do two things at the same time which may be inconsistent. I would like to get this meeting concluded and adjourned, so far as the

acceptances are involved. My theory on that was then we can proceed at more leisure to examine into the other cause. Should it turn out the plan is not accepted, I don't know what the position of the Securities and Exchange Commission would be under those circumstances—

Mr. Scheid: The acceptances seem to be in line. Of course, I don't know what the final result would be.

The Referee: On the present count, there is a slight deficiency in acceptances that can be readily cured by one client of Mr. Maxwell, if time is given to him for that purpose.

I would propose, Mr. Scheid, when March 1st arrives to continue the confirmation hearing as we are obliged to do because of the acceptances would not be determined. What date would you suggest—I want to keep the notice alive on the confirmation hearing so we do not have to send notices again.

(Whereupon, there was a discussion off-the-record after which the following further proceedings were had:)

The Referee: I would prefer to do it this way, to set this for the afternoon—this meeting for the 67 afternoon of March 7th, say at 1:30 and the hearing on confirmation at 2:30 and then on the morning of March 8th, a hearing on the argument on your motion assuming that the arrangements have been accepted.

Is that possible with your calendar?

Mr. Scheid: Yes.

The Referee: Mr. Maxwell, will that afford you the time you think you need?

Mr. Maxwell: That is fine.

Mr. Andrew: Fine.

The Referee: I am still puzzled as to what to do about fixing a cut-off date for the filing of these claims and acceptances.

I am inclined to think if we continued this say—until the afternoon of March 7th—Actually, if Mr. Maxwell's client files his claim properly, it's going to take an awful lot of other claims to offset it so it may not be much more than an adding machine job for the committee to do on March 7th.

Would it be possible for the committee to come here on the morning of March 7th—prior to that time—so that

when it actually comes to the afternoon of March 7th, you wouldn't have but a hand full of claims to consider?

Mr. Maxwell: Yes; we will have to meet during
68 the interval, your honor. We won't be able to count those remainder in that short of time; we would have to have another meeting in between.

The Referee: February 28th was fixed as the last day for the filing of application to confirm; that is going to be continued until March 7th.

I will have to work out a time table here, gentlemen. The one clear understanding we will have, Mr. Scheid, is we won't have the hearing on the confirmation until we have heard your argument.

Mr. Burks: May I suggest the Court set March 8th as the last date of filing petitions so then we will have a firm knowledge of whether the plan has been accepted before we file a petition for confirmation?

The Referee: I will set the hearing at 9:00.

Mr. Maxwell: The cut-off date?

The Referee: No, we are talking about filing of application to confirm. What are your views, Mr. Maxwell?

Mr. Maxwell: That is all right with me.

The Referee: Why don't we try that then and see what progress we could make.

The meeting will be recessed until 1:30 on March 7th.

69 Mr. Scheid, do you want to take some testimony?

Mr. Scheid: Yes, your honor.

The Referee: Mr. Peters, will you come forward, please?

IVAN H. PETERS,

being first duly sworn to state the truth, the whole truth and nothing but the truth, testified on his oath as follows:

Examination

By Mr. Scheid:

Q. Would you state your name, please. A. Ivan H. Peters.

Q. And your address. A. Alliance, Nebraska.

Q. What is your connection with American Trailer Rentals Co.? A. I'm vice president.

Q. How long have you been its vice president? A. Since 1960.

Q. What was your occupation prior to 1960? A. General contracting and engineering—some management services

Q. In this business prior to 1960, did you have any connection with American Trailer Rentals Co.? A. I was a stockholder prior to '60.

Q. Did you have any selling arrangements for or
70 with American Trailer Rentals Co.? A. Yes.

Q. What were those arrangements? A. I had an agreement to sell trailers for American Trailer Rentals Co. in the State of Nebraska, primarily.

Q. You say "primarily," did you sell in any other State?
A. Subsequent to this, I had arrangement to sell some trailers in Iowa.

Q. Where? A. Iowa; State of Iowa.

Q. Did you do this personally or through a corporate entity. A. Through a corporate entity.

Q. Under what name? A. I. H. Peters Co.

Q. Did you have any connection with the corporation named "Executive Sales, Inc."? A. Yes.

Q. What was that connection? A. Executive Sales, Inc. had authority, as I understand it, to appoint sales organizations in the various States. I. H. Peters Co. was selling or directing sales pursuant to the directions of Executive Sales, Inc.

Q. What was your connection with the Executive
71 Sales, Inc. A. When I first started, I had no connection with Executive Sales, Inc. except sales rights.

Q. And when did this situation change? A. It changed about July 1960. I can't recall exactly how or what my capacity was with Executive Sales, Inc. except I was asked to manage some of its affairs from Denver. I'm referring to having an office with this corporation. It seems as though I was named an officer of Executive Sales but I question whether this was accomplished by firm board action. It may have been but I'm vague on this.

Q. You went with Executive Sales; you were not a founder of it? A. No, sir.

Q. Can you tell me who the other officers or directors of Executive Sales, Inc. were? A. Originally, the officers with Executive Sales were Richard J. Rutherford, Jack L. Gribel and David W. Adams. And I believe that was the organization of Executive Sales as it started.

Q. Did those individuals have connection with American Trailer Rentals Co.? A. Yes.

72. Q. What was that connection? A. When I appeared on the scene, Jack L. Gribel appeared as president of American Trailer Rentals Co.; and I believe R. J. Rutherford—I can't recall but he may have been vice president. I don't recall his office.

Q. And David Adams? A. Mr. Adams did not appear as officer of American Trailer Rentals Co.

Q. Was he a director? A. I can't answer that.

Q. Can you tell me at what date you first became associated with American Trailer Rentals Co. or any of its affiliates? Colorado Trailer Rental, Iowa Trailer Rental or anyone. A. I first became associated with American Trailer Rentals Co. late—early in 1959 at a time when I bought stock in that company.

Q. The Debtor was founded on what date? A. Founded in 1958.

Q. And it began to do business when? A. I can't answer that. I wasn't familiar with the corporation until 1959.

I believe they started to do business in November or December of '58 but I gained this knowledge generally through hearsay.

73. Q. And you became associated with American Trailer Rentals after this period—how many months? A. I believe it was in February '59 that I became associated with American Trailer Rentals.

Q. Are you presently a director of American Trailer Rentals? A. Yes.

Q. When did the board of directors of American Trailer Rentals Co. first consider filing a petition under Chapter XI? A. About a month before it was filed. I estimate—I don't recall the date. Perhaps earlier, say—60 days before it was filed. Now, I'm guessing because I don't recall the exact date when we started working on it.

Q. Could you tell me whether you as executive vice president of American Trailer Rentals acted in connection with proceedings brought by the Securities and Exchange Commission regarding sales of the lease-back contracts?

A. Will you state that again, please.

(Whereupon, the Reporter read the pending question).

Mr. Maxwell: I suggest, your honor, that Mr. Peters does not understand the question and that the question be rephrased. I have little trouble following it.

The Referee: In other words—Did you participate in any hearings before the SEC or any of its offices concerning lease-back contracts? A. Yes; I did participate with the hearings.

Q. And was that hearing on January 28, 1963? A. Yes.

Q. At that hearing, did American Trailer Rentals consent to a stop-order with regard to the sale of stock or lease-back agreements? A. Yes.

Q. Was the allegation that there was inadequate disclosure of the use by one or more of the Debtor's promoters of funds raised from the public for other than corporate business, one of the allegations in the Commission's stop-order proceedings? A. I don't remember. I know this was discussed but I don't recall the exact wording of the stop-order.

Q. As an officer and director of American Trailer Rentals Co., were you aware of any possible misuse of corporate funds in the history of American Trailer Rentals Co.?

Mr. Burks: May we have that tied down to a time, please.

Mr. Scheid: 1959 through the present.

Mr. Burks: That is not what I call a "tied down time."

The Referee: He may answer, if he knows.

75 A. I was aware of misuse of funds prior to my active management in the company.

Q. Do you have any idea how much was involved in such misuse of funds? A. No, I do not.

Q. Do you have any idea whether it was a substantial amount or small amount? A. It was substantial amount.

Q. Would you say more than a hundred thousand dollars? A. I doubt that it was more than a hundred thousand but it approached a hundred thousand.

Q. Did you as a director or did the board of directors to your knowledge, take any action against the person or persons who were responsible for this misuse of funds?

A. We didn't because he died.

Q. What person was responsible for the misuse of funds?

A. Well, it was my opinion—unofficially—Mr. Adams was responsible for this.

Q. He is deceased? A. He is deceased.

Q. Did funds come to American Trailer Rentals Co. while you were executive vice president and director, for the purpose of trailer funds from the public which 76 did not go to purchase trailers but went to other purchases in addition to that sum? A. No.

Q. Your schedule filed here show some two hundred six thousand dollars of monies invested by the public for trailers which were not delivered. A. That's true.

Q. Can you tell me the circumstances of that? A. All of those monies were sent—Let me start over.

The monies necessary to purchase those trailers represented by such purchases, were sent to a manufacturer with purchase orders for the purchase of these trailers according to an agreement we had with this manufacturer. The money for the manufacture of these trailers was not retained by American Trailer Rentals Co.

Q. The money went to whom? A. De-Mar, Inc.

Q. Of what State or city? A. Alliance, Nebraska.

Q. And did you have any connection with De-Mar, Inc.? A. I was shown on their board of directors for a time.

Q. At what time? A. From their inception.

77 Q. Which was? A. 1959—I believe May 1959 to sometime in 1960.

Q. Was that early or late in the year of— A. It would have been late in the year.

Q. October, November? A. Possibly. I'm guessing but it seems this was about the time.

Q. And this transaction which you just discussed, the trailers which were not delivered, did this occur during that period? A. No.

Q. When did it occur? A. It occurred in 1961.

Q. At the time of that transaction, did you have any connection with De-Mar, Inc.? A. No.

Q. At the time of that transaction, did any other member of the board of directors of American Trailer Rentals have any connection with De-Mar, Inc.? A. Yes.

Q. What other or how many others? A. William N. Marks.

Q. And what was his relationship? A. He appeared on American's board of directors and president of De-Mar, Inc.

78 Mr. Burks: I will object to this line of questioning. I do not understand where it is leading, and I do not find any provision under Chapter XI wherein this line of inquiry would be relevant to any of the objections to the confirmation of the arrangement.

The Referee: Among other things, under Chapter X the trustee is empowered and is frequently directed to bring causes of action that may have been accrued to a corporation, particularly, through mismanagement.

Am I stating your views, Mr. Scheid?

Mr. Scheid: Yes, your honor.

The Referee: I think the questions are proper, Mr. Burks.

Q. Did any other member of the board of directors of American Trailer Rentals Co. or one of its directors have any relationship to the De-Mar, Inc. organization as an officer, director or shareholder? A. I just stated that, Mr. Scheid. Mr. Marks.

Q. Aside from Mr. Marks, during this period in which you have been associated with American Trailer. A. No. I don't recall that there was any connection with anybody else.

Q. Was Mr. Marks a substantial or small shareholder of American Trailer Rentals Co.? A. He didn't own any shares of American Trailer Rentals.

Q. At what date didn't he own any shares? A. At no time.

Q. Did he have an option to acquire shares? A. Yes; he had option to acquire shares.

Q. And did he ever exercise that option? A. No.

Q. He is not presently a shareholder of American Trailer Rentals Co.? A. No.

Q. But yet, he is on its board of directors? A. No, he is not.

Q. Is he an officer of American Trailer Rentals Co.? A. No.

Q. Was he ever? A. Yes; I believe—I know he's on the board.

Q. Did you ever enter into any agreement with Mr. Marks concerning the control of American Trailer Rentals or the position of board of directors of that company?

A. Are you speaking—asking did I personally or did American!

Q. Did you. A. I was on the board when it was agreed that Mr. Marks would become a member of the board, as I recall.

80 Q. What date was that? A. I believe Mr. Marks became a member of the board in July of '60 and I believe I was shown on the board at that time.

Mr. Marks came on the board to protect his investment because he had given some credit to American Trailer Rentals Co. in order to produce their trailers. And for this, Mr. Marks requested a vote on the board of directors of American Trailer Rentals.

To my knowledge, Mr. Marks never had control of American Trailer Rentals.

Q. At this date in 1960 when Mr. Marks came on the board of American Trailer Rentals Co., were you associated with De-Mar, Inc.? A. Yes; I was at that date.

Q. And what was your position with De-Mar, Inc.? A. With De-Mar, Inc., simply a stockholder; I believe I appeared on De-Mar's board at that time.

Q. Did you sell trailers for De-Mar, Inc.? A. No. Correction—I sold some trailers for De-Mar but they weren't utility type trailers for the use in the American system.

Q. You sold no trailers for De-Mar, Inc. to American Trailer Rentals? A. No; I didn't sell any trailers 81 for De-Mar, Inc. to American Trailer Rentals Co.

Q. Did any of these other corporations of which the Debtor is an assignee have lease-back contracts? A. Well, I sold some trailers for Executive Sales Co.

Q. Arizona Trailer Rental Co.? A. No.
Q. Nebraska Trailer Rental Co.? A. We didn't sell any trailers to the trailer rentals.

Q. To any associate or affiliate of American Trailer Rentals Co.? A. Associate or affiliate?

Q. Yes. A. I assume you are talking about a company or corporation?

Q. Yes. A. I—No; I never sold any trailers to affiliates. Q. Did you sell to any individuals who leased their trailers to any of these companies—Arizona Trailer Rental Co., Nebraska Trailer Rental Co., North Dakota Trailer Rentals Co., Colorado Trailer Rental Co., and South Dakota Trailer Rentals Co.? A. You asked, did I sell?

Q. On behalf of De-Mar, Inc., did you make sales of trailers? A. Not on behalf of De-Mar.

Q. Did you ever receive any commissions from De-Mar, Inc.? A. Yes; I have received commissions from De-Mar.

Q. Under what circumstances did you receive commissions? A. Sales commissions for selling their product, generally camping trailers or fiberglass product. I have received commissions from De-Mar early in De-Mar's existence for helping them. I spent a great deal of time in helping De-Mar get a manufacturing agreement with American and for this I was compensated. This was short-lived and the amount involved is negligible.

Q. At the time you aided De-Mar in getting an agreement with American Trailer Rentals Co., you were also associated with American Trailer Rentals Co.? A. Yes.

Q. What is De-Mar's financial situation at the present time? A. They are bankrupt.

Q. Does De-Mar hold notes of American Trailer Rentals Co.? A. Yes.

Q. What were the circumstances of the issuance 83 of such notes? A. De-Mar manufactured volumes of trailers for American Trailer Rentals Co. and these were trailers that had been—the money for which had been collected from individuals for the purpose of manufacturing the trailers prior to July 1960. De-Mar agreed to manufacture these non-existent trailers which had been purchased by individuals provided there was a pay-back plan or plan to pay for this:

In lieu of this De-Mar would go ahead and make the trailers according to an agreement. In addition, during the development stages of American Trailer Rentals Co. which was all of 1960 and '61, De-Mar was helpful in lending money to American Trailer Rentals Co. to help—keep it growing and promote its growth. This was the only customer De-Mar had.

Q. Did De-Mar, Inc. have an exclusive agreement to manufacture trailers for the Debtor? A. Yes; I believe one was executed.

Q. Do you remember when that was executed? A. It was executed in 1960; I can't remember the date.

Q. Does November 17th sound correct? A. I—It was about that time; I don't know exactly.

84 Q. Were you on the board of directors or an officer of American Trailer Rentals Co. at the time that contract was executed? A. Yes.

Q. What was your connection with De-Mar, Inc. at that time? A. I believe it was just shown as a director at that time.

Q. Did you also act as sales representative of De-Mar, Inc. at any time? A. I did for other products, other than trailers.

Q. In this contract with De-Mar, Inc. for purchase of trailers by American Trailer Rentals Co., would you explain the mechanics of your sales of contracts to the investor and the subsequent use of those funds.

Mr. Maxwell: Your honor, the use of the word "investor" I don't think that is appropriate here.

Mr. Scheid: Creditor.

The Referee: I presume that that is the ultimate fact that is in dispute. I think probably a different word is in order, Mr. Scheid.

Mr. Scheid: We will call them "trailer owners" your honor.

Q. You have testified you sold these lease-back contracts to individuals. A. I didn't on the contract.

Q. You did not sell contracts? A. I sold trailers.

Q. To individuals. A. Right.

Q. At the time you sold the trailer to the individual, did you enter into a simultaneous agreement to lease back that trailer through some other entity? A. Yes.

Q. What other entities did you arrange to have them take the trailers? A. There was a lease drawn providing that the trailer would be leased into a State trailer rental company—the trailer would be leased to a State trailer rental company from the trailer owner.

Q. You mean, one of the companies I named previously? A. Yes.

Q. Were there any other companies on that list? A. I don't recall the list.

Q. Arizona, Nebraska, North Dakota, Colorado and South Dakota? A. Yes; there were others—Iowa.

Q. Any others? A. Wyoming.

86 Q. Any others? A. Kansas. I believe that's all of them.

Q. When a trailer was sold to a resident of Kansas for instance, was the contract then—the lease-back contract assigned, given or made out to a Kansas Trailer Rentals Co.? A. It wasn't made out to them.

Q. The contract would not be made out to say—some other State corporation? A. No; it was within that State.

Q. And that would be in all these other States—this was the method of operation? A. Yes.

Q. At the time those contracts were entered into by the trailer owner, with these various State trailer rental companies, was there any agreement between these several trailer rental companies for assignment to the American Trailer Rental Co.? A. I would say "no" to assignment. I would say that there was an operating agreement, maybe. I don't know the technicality and I never thought of it as an assignment. American had an operating system; the State renting company didn't. The State trailer company had an agreement that American would operate their trailers with the American system.

Q. Why did you undertake this arrangement?
87 A. We felt that—We're selling on local level and in addition, we had a bad need for funds about the time the State trailer organizations were organized and these were set up as franchises and from these we derived revenues for the company. At this time the company had huge operation expenses. We had a man all over at the sending and receiving stations; we had delivery problems; we had great deal of promotional and advertising problems to let the people know there was such a company; we had engineering to do in making good trailers. And by selling franchises provided some revenue.

Q. Did the State trailer company—one of the State trailer rental company—collect funds from the user of the trailer?

A. You mean, was there an isolated one that collected—

Q. Let's take the State of Colorado. Was it normal for Colorado Trailer Rentals Co. to get the funds that were derived from the rental of the individual trailer? A. It was the plan that Colorado Trailer Rentals Co. would be charged certain fees by American for the management of their trailers as provided in the management agreement.

And after these fees were paid to American, then the balance of earnings of a given trailer leased to Colorado Trailer Rentals Co. went into Colorado Trailer Rentals Co. as part of their earnings. It was their source of revenue.

Mr. Burks: May I interject an objection again at this point. I understand the Court's ruling that under Chapter X a trustee may be required to prosecute—I think the Court used the word—in certain instances.

We are concerned here with a motion to dismiss a proceeding under Chapter XI. Before a prosecution could take affect it is necessary for the Securities and Exchange Commission to prove one of the exceptions to the confirmation of the arrangement is in existence and the only exception to which I can see this having any remote relation would be that the Debtor has committed an act which would prevent his discharge from the Bankruptcy Act.

I have no objection to the history of the company since it is a proud history but I do object to dragging out this session—digging here and there on a fishing expedition. This is a hearing on a motion to dismiss a proceeding. I think we ought to confine the questions more strictly along those lines—as set out in the statute which says that "the provisions of the chapter have been complied with" and no questions are being asked on that regard; and
89 "the arrangement is for the best interest of the creditors" and there has been no questions along that line; "that the arrangement is feasible" and there have been no questions along that line;

The Referee: This is Section 328—the hearing we are engaged in.

Mr. Burks: I beg your pardon.

The Referee: Section 328 says in substance that the Securities and Exchange Commission may make application to the Court to dismiss the proceeding under Chapter XI with the privilege of the Debtor if the motion is granted to file under Chapter X. The Debtor has an election either to suffer the dismissal or file under Chapter X. If the Court finds, providing it should have been brought under Chapter X. In effect, the burden is put upon the Securities and Exchange Commission to show the same things—if you move over into Chapter X which provides for voluntary

and involuntary proceedings—the burden is on them to show the same things as in involuntary petition or petitioning creditor would be obliged to show under Chapter X.

On that basis, Mr. Scheid's questions tend to go into those issues.

Mr. Burks: I understand that that was the Court's previous ruling. I am perhaps confused by the procedure. I thought that the Chapter XI provided that

Chapter XI shall be confirmed unless the Court finds any one of the following items—

The Referee: Yes, but Section 328 provides that apparently at anytime—I'm not so sure even after confirmation—the Securities and Exchange Commission could file an application under 328.

But clearly, on the present state of records, Section 328 comes into play. Arrangement has not been accepted or confirmed.

So your objection will be overruled.

Q. Did these State trailer rental companies have offices at any location in their State? A. Yes, in general.

Q. Did you state that you were connected with the Iowa Trailer Rentals Co.? A. Yes.

Q. Where did it maintain their offices? A. We had an office established, as I recall in Marshalltown, Iowa.

Q. What was the function of this office? A. It was for—at that time leasing trailers from Iowa trailer owners.

Q. Was it the headquarters of any sales organization of sales of trailers? A. Yes.

91 Q. Would you state which was its principal business—the sales of trailers or the collection of receipts from the rentals thereof? A. The business of which sales organization?

Q. Iowa Trailer Rentals Co. A. The business of Iowa Trailer Rentals at that time was to lease trailers from people. At that time they were collecting receipts.

The Referee: We will have a short recess at this time.

(Whereupon, after a short recess the following further proceedings were had:)

Q. Were you familiar, as an officer of American Trailer Rentals Co., with all of these State trailer rentals companies? A. Ultimately I was.

Q. "Ultimately"—What date is this? A. Oh—Pick a date in December 1960.

Q. Were you familiar with them before that date? A. Well, I knew some of these existed; I didn't know the status of some of them; I didn't know the principals with the State corporation exactly. But in December of 1960 I was fairly familiar because I had been in the management of the company half a year.

92 Q. Did these other State rental companies, aside from the one you talked about, Iowa, maintain an office in the State whose name they bore? A. Yes.

Q. Did they maintain a staff whose functions were to collect rents and distribute rents to the trailer owners? A. No.

Q. Where was that function carried out? A. That was carried out pursuant to the management agreement which existed between the State and American Trailer Rentals Co. This was set forth in this agreement—part of American's duties according to management, to do certain things.

Q. The State trailer rental companies then were sales organizations? A. No.

Q. What other functions did they perform? A. They were leasing company.

Q. Who sold trailers that these State companies did not? A. Trailer sales was under the direction of Executive Sales.

Q. The Executive Sales, Inc. would sell the trailers and arranged to have it leased to the State companies?

93 A. Agents—representatives of Executive Sales, yes.

Q. Were there any cases where the personnel of State trailer rentals companies differed from that of Executive Sales in that area? A. I don't understand what you mean by "differed".

Q. Different persons involved. In the Iowa system, were you in charge of sales of trailers in Iowa? A. My organization was.

Q. And the organization name was? A. I. H. Peters Co.

Q. And that was operating through a contract with Executive Sales, Inc.? A. Yes.

Q. What was your association then with Iowa Trailer Rentals Co.? A. Personnel of I. H. Peters Co. were empowered to enter into a lease agreement representing Iowa Trailer Rentals.

Q. Did that system pertain to each one of the States?
A. I don't know whether it was; generally, I would assume it probably was.

Q. In making this arrangement whereby sales were made within a particular State and leases executed from the owner to a corporation in a particular State, was any consideration given to an exemption under the registration of the Securities Act of 1933? A. That's a point of law that I'm not—
94

Q. Was it discussed? A. Well, I believe it was discussed. This thing was two-fold. As I explained before, it was getting the necessary capital into this thing and the other was to have intrastate operation.

Q. In gaining the necessary capital, this was to come from trailer purchasers, is that correct? A. I explained we sold franchises.

Q. Sold franchises to whom? A. To the State trailer rental companies.

Q. But the State trailer rental companies were associated with Executive Sales, Inc. A. No; they had an agreement with American.

Q. They had an agreement with American and not with Executive Sales? A. No.

Q. But yet in the Iowa situation, you had apparently the same personnel of the I. H. Peters Co. which had an agreement with Executive Sales as the representatives of Iowa Trailer Rentals Co. A. Representative only in that when a trailer had been purchased, by a trailer purchaser in the State he was executed a lease for that equipment.

95 Q. Did Iowa Trailer Rentals Co. have any other functions? A. No; not at that time.

Q. Not at that time? A. We projected other things for them:

Q. But they did not function in any way? A. Nothing functioned after April 1961 when the SEC stepped in—absolutely nothing.

Mr. Burks: I neglected to note in the objection that I stated. I was going to make the objection that the questions and answers given are beyond the purview of their motion to dismiss—the Securities and Exchange Commission.

The Referee: The objection will be overruled and your exceptions noted.

Q. Can you relate once again, the situation with which you are most familiar with in Iowa—when a trailer was sold to an individual in Iowa he paid a specific sum. Now what was done with that specific sum? Will you please trace the flow of money for me. A. A check or voucher was mailed by the salesman to I. H. Peters Co., their offices in Alliance, Nebraska. That company mailed the money to Executive Sales Co. in Denver, Colorado and they immediately issued a purchase order for that trailer and the funds then went to the manufacturer with the purchase order.

96 Q. And did exactly the same amount that the trailer owner had paid to the salesman go to the trailer manufacturer? A. No; the salesman took a commission.

Q. What were the commissions of I. H. Peters Co. in this particular arrangement? A. I. H. Peters Co. had a total commission of 20%.

Q. Then what was the commission of Executive Sales Co.? A. It varied from time to time. But I believe it ranged from 16 to 17%; on some models of trailers down as low as 5 or 6%.

Q. And then De-Mar, Inc. would manufacture the trailers with this remaining fund, is that correct? A. That's correct.

Q. Was there an excess over this commission that went to any other place? A. Excess over these commissions that we have talked—discussed about?

Q. Yes. Or did all of the remaining fund after commissions go to the trailer manufacturer? A. All remaining funds went to the manufacturer.

Q. Were these commissions geared to take up different trailers—purchase price and the manufacturer's 97 price? A. Yes.

Q. In other words, if the trailer was to cost a thousand dollars, you would add what these commissions would be and charge the owner \$1,000 plus 20% for you and plus 10 to 17% for Executive Sales Co. A. No—backwards. Trailers with established market price was considered and the selling price of the trailers was based on prices of trailers being sold in other organizations. In other words,

U-Haul, Nation Wide, National, Car-Go at that time—there were quite a lot of little companies selling and leasing back trailers and this was based somewhat on the going price—the market price for certain trailers and the quality of the trailers. Then the manufacturing price was established on the basis of the manufacturer's ability to compete and if there was a difference there, this constituted a commission; in addition, there were other manufacturers that made the trailers too, not only De-Mar. De-Mar was competing with them.

Q. De-Mar was competing until— A. We established a precedent on what a trailer would cost of this design and quality and construction.

The Referee: See if I understand this. Assuming the price quoted to the purchaser was \$1,000 for the trailer.

Did the salesman first take off a portion for himself?
98 A. In effect, we did, your honor. The salesman sent in the full amount to I. H. Peters Co. and then I. H. Peters Co. paid that salesman a commission.

The Referee: Was his commission included in the 20% that I. H. Peters Co. received?

A. Yes, sir.

The Referee: And an additional amount ranging high as 17% went to Executive Sales Co.

A. Yes, sir; 17% of the thousand dollars.

The Referee: Theoretically, \$370 could have been deducted and the balance, \$630 would have gone to De-Mar.

A. Depending on the size of the trailer.

The Referee: I am assuming, if it is 20% and 17%.

•A. Ultimately it didn't carry 17%.

The Referee: I was just using this one trailer for example.

A. Yes, sir.

The Referee: De-Mar, Inc. would have received \$630 for its share in that transaction.

A. Yes; that's right.

Q. Now, in tracing these funds, none of them seemed to have gone to any of the State trailer rentals or
99 American Trailer Rentals Co., is that correct? A. In tracing which funds?

Q. The funds we just traced from the trailer purchaser

through I. H. Peters Co., to the Executive Sales Co. and to the trailer manufacturer.

Is it a fair statement that American Trailer Rentals Co. received no funds from the sale of the trailer? A. Money was loaned to American Trailer Rentals Co. from these funds for the development of this system. American had to borrow money to do it from Executive Sales Co.

In other words, American couldn't be profitable until they had a huge volume of trailers. It took a lot of dog and money.

Q. Was the loan—these loans from Executive Sales Co. repaid? A. No.

Q. Is Executive Sales Co. a creditor? A. No.

Q. What is the connection of any officer and director of American Trailer Rentals Co. with Executive Sales Co.? A. There were certain officers who were officers of Executive Sales; certain officers in American Trailer who had nothing to do with Executive Sales.

100 Q. Can you give me the names of directors in common? A. Executive Sales was merged with American prior to our SEC filing in December of 1961. We filed for registration prior to this—Executive Sales was merged.

Q. Prior to sometime in December. A. Prior to that David W. Adams, Richard J. Rutherford and Jack L. Gribel were officers of Executive Sales Co.

Q. As well as officers of American Trailers. A. As well as American Trailer Rentals.

Q. The funds that apparently were misused were these funds of Executive Sales or funds of American Trailer Rentals Co.? A. They were actually Executive Sales but let's establish a date. This was prior to my management of the company. I want this very clear:

As we previously discussed, trailers were sold to individuals and at that time a lease agreement was executed providing that a new lease would be written when the serial numbers of these very trailers were in and effective of that time to allow for the manufacturing time.

Now, certain of these funds were diverted to other things. So this not only left Executive Sales Co. 101 owing trailer owners money, but—

Q. To go back to the Iowa situation, at the time

that I. H. Peters received the money from the trailer purchaser there was a simultaneous agreement with Iowa Trailer Rentals Co. to lease that trailer from the purchaser.

A. Uh-huh.

Q. And to pay him a fixed monthly rental? A. Right.

Q. What was the percentage paid in by the Iowa company? A. 2% a month.

Q. For how many years? A. Ten years.

Q. The only source of income of Iowa Trailer Rentals Co. then was the rents from leasing of that trailer to various persons. The renting of the trailers.

Q. Did they take that money from the rental of that trailer or did that go to American Trailer Rentals Co.? A. After the operational expenses of that trailer were used up. After the operational expenses of a given trailer were paid, anything left over pursuant to this management agreement—this overflow went to the State trailer company.

102 Q. You must bear in mind that we were still in the developmental stage. The last year of '60 we didn't have 3,000 trailers in this system. We didn't have an economical operation—it was spread too thin. And to make it economical we had to—we know what we had to do to make this economical. That's what we were proceeding to do. We started a growth in '60—we had tremendous growth, a great deal of growth. And it looked like this thing was pulling out so the State companies would have a chance to make money. According to the management agreement, American Trailer Rentals didn't give the State trailer companies any money until certain things transpired.

Q. How did it come then that American Trailer Co. appears to owe individuals whose contracts are with Iowa Trailer Rentals Co. When did that occur? A. Iowa Trailer Rentals Co. was merged with American Trailer Rentals Co.

Q. All of these State companies were merged then? A. Yes.

Q. On what date? A. I don't recall the date. But it was the last part of '61; we were advised by the SEC that we could register if certain things took place. That's why we did it; we were anxious to comply with the SEC.

103 Q. How many trailers were manufactured by persons other than De-Mar, Inc.? A. I guess, maybe 500; maybe more or less.

Q. So 90% or more of all the trailers in the system were manufactured by De-Mar, Inc.? A. Uh-huh.

Q. Did you take any salary from Iowa Trailer Rentals Co.? A. No.

Q. Any commissions? A. No.

Q. From I. H. Peters Co.? A. I took a salary from I. H. Peters Co.

Q. Executives Sales Co.? A. No.

Q. De-Mar, Inc.? A. No salary from De-Mar, Ind.

Q. Commissions? A. Some commissions.

Q. American Trailer Rentals Co.? A. My renumeration from American Trailer Rentals is varied. At the time I was asked to come over on somewhat a temporary consultant basis in July of '60 and I was an employe—officer and employe of I. H. Peters Co. And for book-
104 keeping simplicity I. H. Peters Co. received renumeration from—for my services and I still draw a salary from I. H. Peters Co. This has changed, presently changed and I draw directly from American now.

Q. What is your relationship to Capitol Leasing Corp.? A. I am not a stockholder in Capitol; I appear on their board of directors as secretary-treasurer.

Q. Both, officer and director? A. Yes.

Q. Does any other person actively participate in the management of Capitol Leasing Corp.? A. We have a board of directors who meet periodically.

Q. How often do they meet? A. We started at once every thirty or thirty-five days and as the need arise, we call a meeting. We have not set schedule except we don't let it go too long.

Q. This is between the board of directors. A. Yes.

Q. No other persons? A. No. This is discussed by telephone or by correspondence. I consult with the other members of the board even though it's not a regular board meeting.

Q. Does Capitol Leasing Corp. and American Trailer Rentals Co. have any agreement for the use of
105 trailers belonging to Capitol? A. Yes.

Q. What is that agreement? A. American Trailer

Rentals Co. has a system right now and American is managing the trailers for Capitol.

Q. Does Capitol pay anything to American Trailer Rentals for that service? A. No; nothing has been established for payment as yet.

Q. Does Capitol Leasing receive anything or has it received any monies from American Trailer Rentals Co. for this? A. They have received some for the operation.

Q. Can you tell me the last date when Capitol received anything? A. No, I can't. But it's six or eight months ago; maybe four or five months. It's a date I can't put.

Q. At the time Capitol was paid funds for the rental of its trailers by ATR, did American Trailer Rentals Co. owe monies for rents or on lease contracts to other trailer owners? A. Yes.

Q. Why did Capitol receive funds when there were debts outstanding? A. Because, Capitol was organized 106 really to save the investments of lot of people.

Capitol had to have a chance to go ahead; we even registered Capitol under Regulation "A" exemption to get it going so we could get something here to salvage the company. There were other companies too having trailers going adrift—little companies. And Capitol was in—wanted to be in a position to take these trailers under its wing and operate them.

Q. Did you receive any salary or other renumeration from Capitol? A. No.

Q. Have you ever? A. No.

Q. Does American Trailer Rentals have any other arrangement with any person to use their trailers and not charge them any funds—any fee for their services? A. Say it again.

Q. American Trailer Rentals, Co., does it have any agreement with any other persons besides Capitol to use trailers belonging to such person without charging any fee for their services? A. I don't believe so. I don't understand the question, but—

Q. Who is Marvin Young? A. He is the accountant from Alliance, Nebraska.

Q. What is your relationship to him or his relationship to any of these companies? A. Marvin Young was once an accountant for De-Mar, Inc. and

De-Mar, Inc. loaned him to American Trailer Rentals for a period to help us with some internal control problem which existed in American.

Q. Are you familiar with any lease-back agreements from these trailer purchasers to Marvin Young personally? A. I know that Marvin Young set himself up at this time as fleet operator and he has an arrangement with National Trailer Rentals Co. of Detroit, Michigan to place trailers in their system. He is authorized to issue a lease contract for these trailers. To my knowledge, there is nothing about this arrangement that has ever been questioned or registered with the SEC and it's exactly the same thing we are doing, only worse.

Q. I take it that at present he has no association with American Trailer Rentals? A. That's entirely right.

Q. Was he at anytime an officer or director? A. He was shown on the board of directors.

Q. When did he resign or when did he leave? A. About a year ago.

Q. Has American Trailer Rentals Co. ever made a profit?

A. No.

108 Q. Can you tell me what its fixed obligations have been at maximum on these lease-back agreements?

A. Plus seventy thousand a month.

Q. What was the maximum monthly income? A. I don't recall exactly—somewhere in the neighborhood of sixty, seventy.

Q. From the time you have been with American Trailer Rentals Co. did you take any salary from the company? A. From when did I take—

Q. From the time you have been with American Trailer Rentals Co. A. Yes; I already testified that I did.

Q. Was there ever a dividend paid? A. No.

Q. Can you tell me what your monthly figures are right now on the present contracts? A. You mean, on the trailers we now have operating in the system?

Q. Yes. A. I don't know. I don't know how many have been withdrawn from the system. We've had quite a few pirating of trailers out of our system and a lot of these are just in transit to another system and we haven't received

back the release notice that this trailer's transferred
109 from our system to another. I don't know what our obligations would be.

Now, I think we probably—maybe have two thousand trailers yet operating in our system, or maybe three. I don't know. It's hard to determine.

So, if there's two thousand trailers— Probably a million dollars worth of trailers and 2% a month of that would be about what would be paid.

Q. Are you aware of any withdrawals of trailers by any officer or director of American Trailer Rentals Co. and the placement of those trailers in other rental systems? A. Yes; I've been aware of this in one case.

Q: What case is that? A. A Mr. Hammond had some trailers in our system and it seems as though he took part of his trailers and transferred them to the Nation Wide. I'm not sure whether he took them all. It seems as though he left some with American.

Q. Who is Mr. Hammond? A. He appears on our board of directors as "secretary" of American Trailer Rentals Co.

Q. Do you know whether or not Mr. Fritten has transferred to other systems? A. Yes; I know that he has.
110 He's not on the board of directors of American Trailer Rentals.

Q. What is Mr. Fritten's connection with American Trailer Rentals Co.? A. None.

Q. Did you have any discussions with Mr. Hammond about the withdrawal of these trailers? A. Oh, some; his trailers—he could do what he wants.

Q. Is Mr. Hammond also connected with Capitol Leasing Corp.? A. No.

Q. He has no connection at all? A. No.

Colloquy Between the Referee and Counsel

Mr. Scheid: I wonder if counsel for the Debtor would admit the validity of the registration statements.

Mr. Maxwell: Your honor, please. Mr. Scheid has taken the liberty, with reference to an exhibit which he attached to the motion—he attached as Exhibit No. 1 the stipulation of ATR entered with the Commission and this stipulation was for practical purpose entered into by the company

and stated "It agrees that the statement of matters stated on November 27th shall be taken as correct for the purpose of this hearing and no other purpose."

111 We have no objection to the use of the prospectus; it was filed with the Commission in good faith and it was filed with the Commission after the Commission assured that some of the accounting problems would be solved. The accountants for the Debtor conferred with the Commission with reference to this misuse of funds prior to the time Mr. Peters came in. And the fact they could not file an unqualified financial statement, the Commissioners agreed to waive that requirement and actually helped the accountant at the preparation of the statements.

Now, the matters to be considered at the stop-order hearing for the most part involved the accounting, so that the Debtor was then in a position where it could have been assured to have it filed. This stipulation is limited to consent to the correction of the statement of matters for the purpose of that proceeding only. To contest this would have taken days.

The Referee: I take it it cannot be taken as an admission for this hearing and it is limited by its own terms.

Mr. Maxwell: This was filed with the Commission on December 11, 1961 after having received that assurance. It sat there through December, January, February, March, April, May, June and July. The Commission never 112 took any action. In that length of time the Debtor completely changed its condition. It was a true and accurate account as of December 11, 1961. I think the statements in there are at that time true; they are no longer true.

The Referee: It is not clear to me for what purpose you tender this, Mr. Scheid.

Mr. Scheid: The memorandum in support of the motion contains various allegations of fact.* Most of these allegations of fact are contained in the prospectus itself or in the record of this proceeding. There are other allegations concerning Commission proceedings and the documents are attached to show how those proceedings were instituted and what their result was—merely a confirmation of the statement in the memorandum that there was a consent, that there was this statement of matters to be considered

which we believe are serious matters. Now, I am not arguing with the language of the consent. The Commission agreed to it.

The Referee: If counsel does not agree to the reception of these documents, how does the Commission propose to prove it?

Mr. Scheid: I understand we have the agreement on the prospectus. On the others, I will ask Mr. Peters to identify them.

Mr. Maxwell: We have no objection—

113 The Referee: I take it Mr. Maxwell objects to everything except the prospectus.

Mr. Maxwell: We have no objection to the use of the prospectus, but the others we object to.

The Referee: Very well. The prospectus will be considered under the statement of counsel; the others will require proof, Mr. Scheid.

Mr. Maxwell: As a matter of fact, your honor, Mr. Scheid has already gone over the whole story with Mr. Peters; he has hit all the points that he has in his memorandum. There isn't much further he can ask.

The Referee: I am not privy to what Mr. Scheid has in his mind. Maybe he's got a thousand questions.

There is some rule—a statute that certified copies of Commission's proceedings may be received in evidence.

Mr. Maxwell: The Commission's own stipulation precludes them from using it here.

The Referee: It does not preclude introducing it.

Mr. Scheid: These documents are here to show what the basis was for the statement in or memorandum. I have gone through many of the things in the statement of matters which is Exhibit No. 1 attached to our motion; I have not gone through all of them. It is here to show 114 what was alleged by way of showing a need for an investigation by the disinterested person. The fact of the allegations, I think raises a very substantial question. I suppose I could go through and read to Mr. Peters and ask him to state if each sentence is true or false.

The Referee: Suppose we recess until 1:30 and in the interim, you and your associate can consider the best method of proceeding.

Mr. Burks: Mr. Scheid said he suppose he could go through and read every one of the statements. I have no objection to that; I know what the answers are and I am not afraid to put him on the record here.

The Referee: All I can do is when Mr. Scheid resumes, to hear any objections that may be made of what he offers to do and to rule on it. I am not going to anticipate what is or—.

Mr. Burks: I took his statement as an offer and I was accepting it.

The Referee: The offer is not clear and the acceptance is equally unclear.

We will be in recess until 1:30.

(Whereupon, a recess was had until 1:30 o'clock p.m. this same day at which time the following further proceedings were had:)

115 . The Referee: Continue with your examination of Mr. Peters. You understand the oath is still binding on you. A. Yes, sir.

Q. When trailers were sold by American Trailer Rentals Co. or its predecessor affiliate—Executive Sales—did the salesman advise the prospective purchaser that in every case he would arrange to have a lease-back agreement entered into by another company? A. Yes; the lease-back arrangement was executed at the time of the trailer sale.

Q. Did you ever sell a trailer to an individual who wanted to keep that trailer? A. I think in one case.

Q. Perhaps once? A. Uh-huh.

Q. Did any of the trailer owners see the trailers that they acquired? A. No.

Q. They went directly to the leasing system upon delivery? A. To make money and they had to go where the trailers were needed, generally away from these people's home.

Q. I believe you have stated that you attended a hearing on January 28th before a trial examiner in the offices of the Commission here in Denver? A. Yes; the Securities and Exchange Commission.

Q. At that hearing, I believe you stated that the Debtor consented to a stop-order? A. Yes.

Q. For the sale of these lease-back agreements by American Trailer Rentals Co. A. We consented at— to a stop-order; we never resumed sales after April 12, 1961.

(Whereupon, documents were marked Sec:s Exhibit A, B, C & D.)

Q. Mr. Peters, I hand you what has been marked SEC Exhibit B and ask you to read that, please.

Is SEC Exhibit B a copy of a consent to a stop-order which you executed on January 28, 1963?

Mr. Burks: May we have the witness identify it?

Q. Would you identify the document. A. It's entitled "Consent to Stop-Order" and it's a photocopy; place for my signature but that didn't copy. I don't remember the wording of the document I originally signed but I would assume that this is a copy of the one.

Q. I hand you what has been labeled SEC Exhibit A and ask you to look at that. A. Are we talking about the first page or each page?

117 Q. Each page. A. Each page.

Q. Can you identify SEC Exhibit A? A. This was an order fixing the time and place for the hearing which has been held.

Q. You had received a copy of such an order in advance of that hearing? A. Yes; this appears to be a copy of it.

Q. In addition to the order you received a statement of matters to be considered which is also a part of that exhibit. A. It appears the same.

Q. The same statements so far as you know? A. As far as I know.

The Referee: Do you offer Exhibit B in evidence?

Q. I am going to in a minute.

Do you remember signing a document of which SEC Exhibit B is a photocopy? A. I remember signing a document; I assume it's a copy of the same document.

Q. And do you recall at the same time your attorneys Maxwell and Burks signed the document with you? A. I don't recall whether they signed it or not; I am aware I signed a document.

Offers in Evidence and Objections Thereto

Mr. Burks: We object to the admission of Exhibit B. By its own terms it proves nothing because it is a stipulation as to a stop-order which Mr. Peters has already stated was entered against the company and it goes on to say that the statement of matters dated November 27th shall be taken as correct for the purpose of this hearing and no other purpose.

It is improper to admit the consent and stipulation in this hearing; it has no probative value.

Mr. Scheid: It is being admitted only for the purpose of shown such a consent was entered into and we offer the statement of matters as to this consent directed to show the allegations that were made in the proceedings and the manner in which the proceeding was concluded.

I do not believe we have a Commission order on it yet but I believe that follows in due course.

Mr. Burks: Your honor, counsel for the company Mr. Maxwell has of course admitted the entry of the stop-order, and I do not think there is anymore proof necessary on the matter.

The Referee: Mr. Scheid, I cannot concede that they have any evidentiary value here.

Mr. Scheid: I think the evidentiary value is certainly not as to the truth of the allegations contained in the statement of matters or in this Exhibit B.

The evidentiary value is to show that various 119 allegations have been made regarding American Trailer Rentals Co.; that this situation was brought to the attention of the company; their response to these allegations was that they consent to a stop-order in the order of—

Mr. Burks: Our response to these matters was an answer and I object to that.

Mr. Scheid: This is true. They denied the allegations but—

The Referee: I am going to sustain the objection but make the exhibit a part of the record, Mr. Scheid, so that it may go up with my report.

Mr. Scheid: We offer Exhibit A at the same time, your honor.

Mr. Burks: Of course, your honor, we will make the same objection to this as to the previously offered exhibit, being that this is a statement of matters to be considered at a hearing and they have no probative value here whatsoever. I think that evidence is before the Court and admitted by counsel. I don't think we need to go into the matter any further.

The Referee: Objection is sustained but the exhibit will be made a part of the record.

Q. I hand you what has been marked SEC Exhibit C.

You have testified, Mr. Peters, that you are an 120 officer of Capitol Leasing Corp. A. Yes.

Q. You are not a shareholder, is that correct? A. That's correct.

Q. Capitol is the corporation which is to issue securities under the plan of arrangement proposed in this proceeding, is that correct? A. That is correct.

Q. Under that proposed arrangement, will you receive any securities of Capitol? A. Yes; in lieu of money American Trailer Rentals owes me and I would be eligible for treatment as any other creditor.

Q. Are you familiar with the affairs of Capitol in-so-far as they involve Commission proceedings? A. Yes.

Q. You attended a hearing with regard to Capitol on January 28, 1963. A. I attended a hearing; I don't recall on that date whether we were discussing Capitol or American Trailer Rentals. I know we had a hearing held in both.

Q. Did you receive what has been marked SEC Exhibit C? A. Yes.

Q. Could you identify what has been marked SEC 121 Exhibit C. A. Yes.

Q. Could you tell me what it is? A. It's an order temporarily suspending—exemption statements of reason therefore and notice for opportunity of hearing.

Q. That document is from the Commission? A. Yes.

Q. Did you receive a copy of that document? A. Yes, I believe I did.

Q. The issue stated in that document are those which were before the hearing examiner at the hearing on January 28, 1963. A. Yes.

Q. Did Capitol respond to that document? A. You mean, did they attend the hearing?

Q. Did they answer the allegations contained therein?

Mr. Burks: Your honor, I object to the line of questioning concerning Capitol Leasing Corp.

The motion of Securities and Exchange Commission to dismiss in the second paragraph states as follows: "Said proceedings should have been originally brought under Chapter X of the Bankruptcy Act because the Debtor's circumstances and capital structure are such that the relief afforded by Chapter XI are inadequate as such."

122 There are no statements in there concerning the structure, the actions or past history of Capitol Leasing Corp. and I object to the Commission going into it at this time.

The Referee: Objection is overruled.

A. This is a legal term that I am not familiar with. What do you mean by "respond"?

Q. You did not admit the allegations contained in that document, did you? A. Certainly not.

Q. The matter was heard by the trial examiners? A. Yes, it was.

Q. And the matter has not yet been determined? A. As far as I know it has not.

Offers in Evidence and Objections Thereto

Mr. Scheid: Your honor, I offer SEC Exhibit C to show the matters at issue in the hearing involving Capitol before the Commission as relevant to this proceeding since Capitol is the issuer of the securities herein.

Mr. Burks: Your honor, I object to the admission of this document in evidence for the reasons that I have previously stated in regard to the line of questioning which was going on;

Also, for the reason that as the witness testified these matters are at issue at the present time before a 123 hearing examiner of the Securities and Exchange

Commission; they have been denied; and there has been a full hearing on them and there has been no determination of the hearing—that is, no determination as to the correctness or incorrectness of these allegations.

Therefore, they are irrelevant, immaterial and they have no probative value.

The Referee: What is the purpose of the document?

Mr. Scheid: The Commission feels, the Court should certainly consider the problems of Capitol in view of the fact that they are the issuer of more than a million shares of their stock under the proposed arrangement in this particular case. I feel this is a substantial question.

I am not alleging in this hearing that all of these things are true. I think I will bring several of these things that are true to your attention that are important.

But I believe that the Commission's order to Capitol to appear and its order temporarily suspending an exemption is important in view of their issuance of large blocks of securities.

The Referee: Is the position of the Commission that if the arrangement were approved and confirmed, that Capitol could not issue the securities?

124 Mr. Scheid: I believe it is the position of the Commission that there is an exemption offered in 393A of Chapter XI from the registration requirements of Section 5. I do not believe that the Commission contends that that does not exist—I believe it could be issued.

The Referee: Is this offered solely for the purpose of showing that the Commission engaged in an investigation of the issuance by Capitol of securities?

Mr. Scheid: As well as showing that it has taken this step, that there has been a hearing and it is at issue. That is as far as I go.

The Referee: So limited, I will admit the exhibit.

Mr. Burks: Well, of course, there has been a hearing in the matter and—

The Referee: Admission on those terms amounts to the same thing.

Mr. Scheid: I believe we are having no trouble with SEC Exhibit D which is the prospectus. I would like if possible, to substitute a photostat.

The Referee: Exhibit D will be admitted and a photostat copy substituted.

Mr. Burks: I have no objections to the substitution.

Mr. Scheid: It will be a clear copy.

Mr. Burks: It will be a clear copy; all right—
125 then we have no objections to the substitution.

We have no objection to the admission of SEC
Exhibit D.

The Referee: Very well; it will be admitted.

Q. The plan-of arrangement filed herein shows debts due to officers, directors and large shareholders on promissory notes totaling \$285,277. Are you familiar with those loans? A. Yes.

Q. Were those loans made in cash? A. Yes.

Q. Were all funds received by American Trailer Rentals Co? A. Yes; I believe they were. I can't be certain but I believe they were.

Q. Who else might have they gone to? A. Might have gone to Executive Sales at one time but if so, it was as probably prior to my association with the company in the management capacity.

Q. Is any of this amount due you? A. Yes.

Q. When did you make loans to the company—to the Debtor? A. Within the last year.

126 Q. After January 1, 1962? A. Yes.

Q. Did the other officers and directors so far as you know make their loans at the same time? A. No. Some of them made loans prior to this and some made loans after this.

Q. Does the Debtor owe you any money for services? A. Yes.

Q. And did you file a claim for that amount? A. Services that the Debtor owes me money for have occurred since November 1—we have set a cut-off date of November 1 in compiling our accounts payable by the company. And I've been little too busy to be concerned about this—I'm concerned about it but I haven't had time to do anything about it.

Q. Can you tell me generally for what purpose these loans were made? A. Yes. They were operating funds for the company and they wouldn't have been made had we known that SEC would never register us.

Q. Were any of these funds paid out to trailer owners pursuant to contract? A. Yes; some of them went for us.

Q. Were any funds paid to other trailer owners pursuant to these contract? A. Did you ask were some paid in by trailer—

127 Q. Were funds of one trailer owner paid to another by way of 2% or 3% return on investment? A. To give you a "yes" or "no" answer, I'd give you an unclear answer. Would you like me to answer the best I can?

Q. Please. A. We had three sources of revenue during the period just before the SEC entered the picture in April 1961.

One was the commissions—what was left with Executive Sales Co. and loaned over to American. This was the developmental fund; we had to live with trailers and we had operational expenses of that nature.

Then we had earnings of the trailers themselves. During this developmental stage we knew we didn't have enough income from this group of trailers at that time.

And the third source of funds was from loans by officers who had faith in this thing and they were conscientiously trying to make it work.

So, any way you ask it—yes, maybe trailers earned some money and that money went into the fund that paid trailer owners according to their lease agreement.

Q. Would the funds in this pool of fund that were paid out on these contracts to trailer owners, would this pool include funds that were paid in by some trailer 128 owners in payment for their trailers? A. We have established that there was—some of the commissions went to Executive Sales Co. which was in turn loaned over to American by Executive Sales Co.

We didn't have a special place for special money. We had growth problem—we were trying to accomplish the best we could.

Q. After the merger of Executive Sales into American Trailer Rentals Co., did any of the funds collected from the trailer purchasers go to the payment of debts due other trailer owners? A. Well, Executive Sales Co. was merged with American Trailer Rentals Co. after April 12, 1961 and we had no further sales. This merger took place after the SEC stepped in.

Q. Prior to April 1961 the funds of Executive Sales retained by them as commission were loaned to American Trailer Rentals Co. A. Yes.

Q. And American Trailer Rentals Co. used these loans to pay the 2% or 3% on the contracts? A. They used them for the whole operating fund wherever the money was needed—some would go to that, some would go to salaries, hauling expenses and some went to pay insurance premiums.

129 Q. Do you remember how much you paid out to present trailer owners according to the schedule filed in this proceeding? A. No, I don't recall what it was.

Q. Approximately \$330,000? A. This could be accurate. It doesn't ring a bell with me. I don't have this in my mind.

Q. Did the Debtor's income from the rental of trailers to your knowledge equal \$300,000? A. When?

Q. I am speaking during the time you were connected with American Trailer Rentals Co. A. I'm still connected with American Trailer—

Q. Yes. A. You mean, did we take in \$300,000 in operating revenues?

Q. Yes. A. Oh, yes; I believe we did.

Q. What were the expenses of operations of that return? A. Operating expenses exceed that return, obviously.

Q. Did they exceed that return by including or crediting amounts due these trailer owners on their contracts exclusive of the amount due them? Did the corporation have a net income, in other words of \$300,000 during this entire period which you were associated with the company? A. No; they didn't have net income.

130 Q. Can you describe the method of operation of American Trailer Rentals Co. in detail? A. The mechanical aspect—

Q. The way you keep track of the trailers. A. Each trailer has its own activity card and each station or agency which rents trailers has a code number.

Each trailer is identified by a serial number and this card shows this serial number, and the size, and style of the trailer.

Anytime a trailer makes a movement, on the activity card is logged the sending station and receiving station of each rental transaction.

We also have local rentals of trailers which—some to be used in the own community and returned to the originating station. In such cases, it just shows the local rental.

Each station agency receives a commission or percentage of the rental for handling our trailers and for being our dealers. For this commission, he is required to do certain things, such as keep some records, mail copies of his rental contract to our office, to the receiving station 131 and retain one for his own files. In other words, to keep track of every trailer he rents. On each Monday, he is required, according to the agreement we have with him, to remit to our office through the mails, payment for the amount of rentals that he has conducted the previous week, less his commission.

Q. Is that system presently in operation? A. It certainly is.

Q. Are funds presently coming into American Trailer Rentals Co.? A. Funds are coming in.

Q. Can you tell me what the average amount is, per week or month? A. That is difficult. This is a seasonal business. At what period?

Q. Last week or last period which you can report. A. Last week, probably— six hundred. I don't know what amount— what the total was last week.

Q. What was it say a month before you filed the Chapter XI petition? A. As I recall, \$14,000 come in and following that, it was down to sixty-five hundred.

Q. You have testified that it was sixty thousand at 132 its peak. A. I believe it was approximately that.

Q. As a director of American Traieri Rentals Co., did you in a board meeting consider the formation of a corporation to do what essentially what Capitol Leasing Corp. is proposing in this proceeding? A. We discussed arrangement by and under Chapter XI at the board meeting.

Q. Did you discuss formation of a corporation which was to do what Capitol Leasing Corp. is doing in this proceeding? A. Oh, yes. We discussed all sorts of things. We tried to work out an agenda but— We discussed all kinds of varied ideas.

Q. Who formed Capitol Leasing Corp.? A. It was formed by nine persons who are shown in their offering circular which we filed under Regulation "A" showing these people being the incorporators of Capitol Leasing Corp.

Q. Was this formation accomplished at the suggestion of the directors of American Trailer Rentals Co. or a director of that company? A. Well, I was one of the incorporators of Capitol Leasing Corp. and we saw that it might be a solution to salvage the interests of some of our trailer owners.

We also had very firmly in our minds that if we could go ahead with Capitol Leasing Corp.—on its proposed course that we laid out by the originators of this corporation, that it could grow and prosper, provided it didn't have a stop-order or interference by some other agency of the government. We didn't anticipate any problems—the extreme problem with the SEC before anything was filed. The people in our regional office will testify to that.

Q. Would you say that Capitol Leasing Corp. was formed primarily for the purpose of issuance of its securities through this proceeding? A. No; it wasn't organized for the issuance through this proceeding.

Q. Can you tell me what it intended to do aside from this? A. Aside from what?

Q. Aside from the issuance through this proceeding. A. Well, when Capitol Leasing was formed, we had no idea that we'd ever file anything—of any corporation under Chapter XI.

Q. Your petition states that Capitol Leasing has 299 trailers, is that correct? A. That's correct.

Q. Those were trailers which were in the American Trailer Rentals Co. system, is that correct?

134 Q. Did Capitol Leasing Corp. intend to gain other trailers? A. Yes.

Q. How was it going to gain other trailers? A. By issuance of stock for those trailers as provided in the offering circular prepared and issued by Capitol Leasing and filed under Regulation "A".

Q. Weren't there 388,000 shares of Capitol Leasing Corp. issued pursuant to that offering circular? A. Yes.

Q. Are you familiar with the limitations under Regulation "A" of \$300,000? A. Yes.

Q. Can you tell me how you intended to get the next two million dollars worth of trailers? A. We were speculating on a full offering. Of course, this was changed

when market conditions went down in May of last year and it seemed impossible after that occurrence to have much success in selling new stock—issue stock for a new company.

Q. In issuing these securities of Capitol Leasing Corp., you state in the plan of arrangement that stock was issued for trailers having the original cost of \$176,665.93. By staggering the cost, do you mean the amount paid by 135 the trailer owner including commissions? A. Right.

Q. So that the value of trailers would be somewhere between 30% and 37% less than that amount?

Mr. Burks: I object to that.

The Referee: The witness may answer, if he knows.

Mr. Burks: This is a statement by counsel in the nature of leading question. I will submit Mr. Peters is his witness. He said the value of the trailers would be such and such and between such and such. I don't think that is a proper question on direct-examination,

Mr. Scheid: I will withdraw the question. I think it's just a mathematical computation from previous testimony.

Q. In your plan of arrangement, Mr. Peters you state that you owe on these fixed percentage of lease-back agreements in a sum in excess of \$710,000. A. Did you say 6%?

Q. On these "fixed percentage" I said. A. Oh, yes; I understand.

Q. That there is remaining capital investment for these people of \$1,500,000 and something in excess of that. You are issuing securities for the \$1,500,000.

Is there any provision in the plan for the payment to any individual trailer owner who has withdrawn a trailer prior to the filing of the proceeding?

136 Mr. Burks: I object to the question. I do not see what it is directed at unless it might be a provision of the law which has been repealed and which is that the plan must be fair and equitable, which of course is no longer the law. I can't see how the question could be directed to anything else but—

Mr. Scheid: All I am trying to find out is have they shown all their debts.

The Referee: The objection is overruled. You may answer.

A. What was that again?

Q. At the time of withdrawal of trailers from the sys-

tem—and apparently some 2,800 trailers must have been withdrawn—did you owe any individuals any money? A. Yes; lease payments were not current.

Q. At the time of the withdrawals, was there a release of any obligations due by American Trailer Rentals Co. to these individuals? A. Was there a release of our obligation to them?

Q. Yes. A. Yes; there was.

Q. In every case? A. To my knowledge, there was in every case.

Q. Do you have copies of those agreements with you?

Mr. Burks: No.

137 Q. At the time of the withdrawal of trailers, was there any effort made to determine the value of that trailer? A. At the time of the release?

Q. At the time of the release? A. By whom?

Q. By American Trailer Rentals Co. or by the individual owner.

Mr. Burks: I don't see how the witness can answer for an individual owner. He could answer whether the company tried.

The Referee: He may answer, if he knows.

A. I don't know.

The Referee: Let's answer about the company.

A. The company certainly has a rule of thumb for the value of these trailers. We know how they were constructed—supervised the construction of them. They are "Husky" all steel trailers and we don't have any wooden trailers. They're all welded construction. We know their life, know the depreciation allowable on them; we know about the tire wear—what it is per year on a trailer. We know what these things are worth.

Q. At the first meeting of creditors which I believe was February 1, 1963 did you testify that debts due individuals who have withdrawn trailers might exceed \$1,000,000? A. I don't remember what I testified there.

Q. Do you recall questions concerning \$1,000,000?

Mr. Burks: I think counsel is taking this out of context. The question was concerning itself with the potential liability for whatever rejection of the executory contracts which is not—

The Referee: That is your version of what was done at the first-meeting.

Mr. Burks: I just thought I might assist counsel in straightening out his question.

The Referee: Do you want the question read? A. Yes.

(Whereupon, the pending question was read by the Reporter.)

A. I don't remember.

Q. Does the plan of arrangement provide for the payment of any monies that might be due persons for the rejection of these what are described as executory contracts?

A. Provide payment to people who withdrew trailers—no.

Mr. Scheid: Your honor, I think I am through with the witness.

In our memorandum, we relied a great deal upon what was said at the previous hearings and upon documents which I have filed by the Debtor or by creditors. For instance, on the allegations in our memorandum on 139 the payments due and terms of these contracts. It's been from looking at claims filed and seeing what these contracts—that some of the people sent in had to say.

The Referee: I don't believe those are before me unless—they are made a part of the record on this hearing.

I realize the problem involved in assembling the record but I don't think that is a burden that can be escaped.

I propose to continue this hearing until—I think it is the 8th, so that you will have an opportunity to compile those things. I don't want to terminate the hearing today because I want to give everyone—and your opponents a chance for rebuttal or whatever they may arrive at.

Mr. Scheid: That would be satisfactory to me. I could go through—I think Mr. Peters is probably familiar with those particular contracts and terms.

The referee: Why don't we take a short recess.

(Whereupon, after a short recess, the following further proceedings were had:)

The Referee: You may proceed, Mr. Scheid.

Q. Are you familiar with the types of contracts issued

by the various State trailer rental companies—the
140 lease-back contracts from individuals? A. Yes.

Q. Were these in the Arizona Trailer Rentals Co.—the contract, all for the same term or for differing terms? A. Some of them were for different terms down there.

Q. Would they be five years as a minimum? A. I don't recall exactly but this could be right. I know they differed from the contracts used in some of the other States.

Q. Did all of the Arizona Trailer Rentals Co. contracts call for 3% of gross rentals? A. Yes.

Q. Would the various kinds of contracts be true for the State of Nebraska, North Dakota, Colorado, South Dakota, Iowa, Wyoming and Kansas companies? A. No, it wouldn't. Arizona was kind of a testing ground for developing a sales and trailer procurement program. The other States with trailer rental companies were incorporated after this and they were—all of their contracts were uniform—of uniform nature.

Q. These remaining contracts were by and large for a term of ten years at 2% per month. A. That's correct.

Q. And all of these contracts became the obligations of American Trailer Rentals Co. through merger? A. Yes.

Mr. Scheid: Your honor, we have relied on a great deal—on the memorandum—is the proposed plan filed by the Debtor, its petition for arrangement and its schedules. We have relied on the truth of the allegations and I believe—

The Referee: Of the schedules and arrangement; certainly, I will take notice.

Mr. Scheid: In the memorandum itself, we have in the first paragraph of page six at the end of the paragraph the date "March 27, 1962" and that should be October 9, 1962.

The Referee: My file with the Commission's memorandum is in that pile there. You may have leave to make the change.

Mr. Scheid: And on page seven in the first full paragraph and the fifty line from the bottom, the figure \$361,833.15 is shown and it should be \$361,733.15.

The Referee: You may have leave to correct that by interlineation.

Mr. Seheid: I have no further questions of this witness.

The Referee: Do you desire to examine the witness at this time, Mr. Burks?

142 Mr. Burks: I desire to make a motion at this time.
The Referee: Very well.

Mr. Burks: I should like, of course, to examine the witness but having been through this—played the same record about three times in investigations in front of the Securities and Exchange Commission, I can pretty well judge my time elapsed in my performance. I'm sure it will be close to three-quarters of the day. And that is cutting a lot of the frills out which I provided the Securities and Exchange Commission.

The Referee: You may state your motion.

Motion to Strike From the Record Certain Evidence, Etc.

Mr. Burks: I would like to move at this time to strike from the record all—and have the Court refuse to consider—matters relating to the history of the company in regard to investigations by the Securities and Exchange Commission, in regard to statements of the misappropriation or misapplication or misuse of funds at the inception of the company relative to position of the directors of American—on the board of American, at the time they were serving on the board as officer or employee of any other company including De-Mar, Inc., including Executive Sales or any other so-called State companies.

I would move to strike all evidence which does not tend to prove lack of any of the elements which are necessary to the confirmation of this matter. And I would
143 state to the Court my reasons therefore as follows:

Counsel made the statement that the reason for introducing all of this evidence is for the purpose that under Chapter X, that it may be the duty of a receiver or another officer of the Bankruptcy Court to bring charges or see that charges are brought against the company or its officers or directors.

I would submit to the Court that that is beyond the purpose for which Securities and Exchange Commission is permitted to intervene in a Chapter XI proceeding.

The statute in this regard says that the judge upon the application of the Securities and Exchange Commission and upon notice may direct if he finds that the proceedings should have been brought under Chapter X of this Act, enter an order dismissing the proceedings under this chapter—in paraphrasing—unless the Debtor or one of the creditors of the Debtor files a Chapter X proceeding or amends this proceedings.

I submit that it is improper for the Securities and Exchange Commission to introduce any evidence which might indicate that prosecution should be brought against any of the officers, directors or the company itself; that 144 the only thing they are permitted to do is to suggest to the Court by testimony, if necessary, that this should be a proper proceeding for a Chapter X and not under Chapter XI. It is improper for them to suggest that it should be a Chapter X because prosecution may be necessary. This is not within the purview of this particular section of the Act.

The Referee: Mr. Burks, I believe you are misusing the words that this Referee employed earlier today.

When I referred to "prosecution" I did not mean prosecution by criminal authorities; I meant action which would be—civil action which would be prosecuted by—under a Chapter X trustee if one were appointed.

If I gave the impression that I was dealing with criminal matters, I want to say, counsel, that I did not intend to do so. I am not concerned in this proceeding whether or not there was criminal liability, although—and undoubtedly it would be the duty of the trustee if he found evidence of criminal liability to submit it to the United States attorney or other criminal prosecuting attorney.

But, I used the term "prosecution" in the sense of commencement of civil action.

Mr. Burks: I have other grounds upon which—

The Referee: I wanted to clear that up so you 145 would not be under misapprehension.

Mr. Burks: You not only cleared it up; you closed the subject.

The Securities and Exchange Commission failed at this time to elicit from any of the exhibits before the Referee

any reason why this should not proceed as a Chapter XI arrangement proceeding.

The Referee: I am sorry to interrupt you again—But the Commission has not rested its case.

Mr. Burks: I thought you said—

The Referee: He said he had no further questions of the witness.

Mr. Burks: Have you any further witnesses?

Mr. Scheid: I had rather anticipated these contracts be part of the evidence—have to put them in somehow. We do have an argument that perhaps we are dealing with secured creditors. I think the various contracts had better—

Mr. Burks: How does the Securities and Exchange Commission propose to—

The Referee: I was going to continue this until March 8th at 9:00 a.m. Any evidence that counsel desires to offer at that time may be offered. Mr. Burks, of course,

I will hear any motion you make and if I overrule 146 them, you may offer any testimony and if I sustain you, the matter is then ready for report and disposition by the judge.

Mr. Burks: Then pending our further hearing on March 8th, since the Commission has not closed, I do not propose to open my case at this point.

The Referee: I thought, if you wanted to you could examine Mr. Peters now. I am not requiring you to do so.

Mr. Burks: No. I should point out to the Court that regardless of your statement and explanation as to what I said before the Court—the motion to strike all of the evidence which does not—

The Referee: That motion will be denied without prejudice to its renewal when the Commission rests, Mr. Burks.

Mr. Burks: Thank you.

The Referee: Is there anything further we can do this afternoon? If not, then the first meeting will be continued to March 7th at 1:30 p.m.

An order will be entered as of this date that the application for confirmation shall be filed on or at, or before 8:30 a.m..

I propose that on March 1st when the application for confirmation is set for hearing, on that day I will enter

a minute order continuing that proceeding until
147 March 8th. As I explained earlier today, the purpose of this is to keep the notice alive. This hearing we are conducting now, Section 328 hearing will be continued to March 8th at 9:00 a.m. I am going to strike from the calendar—vacate rather, the order that the application to confirm is to be filed on or before March 7th.

Mr. Scheid: I assume then on March 8th the hearing on confirmation will once again be continued since we will have a better idea on that date—

The Referee: Yes. What I am trying to do is keep all of these things bunched together so that no matter what happens, the Court will not have to be standing still for a long period of time just waiting for a date to arrive.

Mr. Burks: May I check my dates and time March 7th, 1:30, first-meeting.

The Referee: Right.

Mr. Burks: March 8th, 9:00 o'clock continuing the hearing on the motion to dismiss.

The Referee: Right.

Mr. Burks: Will it be necessary for the Debtor to appear on March 1st—I believe it was set originally?

The Referee: No. I don't see any necessity because I propose to do it on my motion whether any one is here or not.

Mr. Burks: Thank you.

The Referee: Thank you, gentlemen.

(WHEREUPON, the proceedings ended.)

(Reporter's Certificate to foregoing transcript omitted in printing.)

149

(Filed Mar. 18, 1963)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

IN BANKRUPTCY NUMBER 33276

In the Matter of,

AMERICAN TRAILER RENTALS COMPANY, *Bankrupt.*

(Filed Apr. 17, 1963).

Transcript of Proceedings—March 8, 1963

The above-entitled matter came on for hearing upon the motion of the intervenor to dismiss before the Honorable Benjamin C. Hilliard, Jr., Referee in Bankruptcy on the 8th day of March, A. D., 1963, in the City and County of Denver, U. S. Post Office Building, at the hour of 10:00 o'clock.

Appearances:

On behalf of the Bankrupt:
Gilbert Maxwell, Esq., and
Arthur W. Burke, Jr., Esq.

On Behalf of the Security and Exchange Commission:
William D. Seheid, and
William J. Conney, Esq.

150 On behalf of some of the creditors:
Martin J. Andrews, Esq.

On behalf of some of the creditors:
Joseph C. Jaudon, Jr., Esq.

Colloquy Between the Court and Counsel

WHEREUPON, the following proceedings were had, to-wit:

The Court: Mr. Maxwell.

Mr. Maxwell: If it please the Court, the Application for the Confirmation has been filed last evening.

The Court: Yes, it is before me here. I would like counsel to refresh my recollection. Was this matter continued for two purposes? One for consideration of the application for confirmation and the other is the continued

argument on the Section 328 motion filed by the Security and Exchange Commission?

Mr. Scheid: That is my understanding, Your Honor.

The Court: I am going to postpone consideration of the application for the timebeing and permit Mr. Scheid to go ahead with his case under Section 328.

Mr. Scheid: Your Honor, I have one matter and one matter only.

151 If Mr. Peters will resume the stand, I think we can take care of it.

(Security and Exchange Commission Exhibit "E" was marked for identification.)

Mr. Scheid: Mr. Burke, is it fair to say that what has been marked as Security and Exchange Commission's Exhibit "E" contains the wording of the usual contract issued by American Trailer Rentals Company?

Mr. Burke: This is a typical two percent lease. The greater majority of our leases are two percent leases.

Mr. Scheid: And this is typical of those contracts?

Mr. Burke: Yes, that is correct.

Mr. Scheid: We would like to have that admitted.

The Court: Very well, by stipulation, it is admitted.

Mr. Burke: May we substitute that exhibit with a photostatic copy?

The Court: One thing at a time. By stipulation of the parties, Exhibit "E" will be received, and by stipulation, the SEC will be permitted to furnish us a photostatic copy in lieu of the original.

152 Mr. Burke: I have no further witnesses or evidence, Your Honor.

The Court: Is there any evidence or witnesses on behalf of the debtor?

Mr. Burke: We have no matters to bring up at this time. I am not clear at this moment as to the position of the Security and Exchange Commission, that is, their specific position as to the dismissal. Their motion is a rather general motion and their memorandum is a somewhat shotgun memorandum, and I should like to know what their position is, so that we know specifically on what grounds they propose to dismiss the proceedings.

The Court: I assume without knowing that they depend on the exact language they employed in their motion, Mr.

Burke. If it lacks clarity to you, why, you are certainly entitled to argue with that in that regard. If you will state your position, perhaps Mr. Scheid could enlighten you. I don't know.

Mr. Burke: The motion of the Security and Exchange Commission to dismiss in the second paragraph, states that: "Said proceedings should have been originally brought under Chapter Ten of the Bankruptcy Act, because the debtor's circumstances and capital structure are such that the relief afforded by Chapter Eleven is inadequate."

I am not—it is clear to me what capital structure is. I presume that they mean the number of shares and the number of shares outstanding, which is my understanding of the capital structure. The circumstances, I don't understand. As the Court knows, this is a rather nebulous sort of an area at the present time by the Exchange Commission. It was first laid out in their realty case and subsequently the right to intervene for the purpose of making a motion to dismiss was set forth in the statutes. So we are dealing in a rather nebulous area, and I think the evidence adduced by the Security and Exchange Commission has made it even more nebulous. I am not at all aware of what direction they are going, and upon what ground they are proceeding to move to dismiss.

The Court: Mr. Scheid, do you want to endeavor to enlighten Mr. Burke?

Mr. Scheid: The motion, Your honor, is based upon Section 328 of Chapter Eleven. Our motion states, that the relief afforded by Chapter Eleven is inadequate to satisfy the needs to be served, and that sentence in the motion in the second paragraph is more fully set forth in the memorandum in support of this. I think our memorandum does give an explicit statement what we believe our reasons to dismiss the proceedings are and in accordance with our motion. There are additional facts, 154 and I am prepared to argue this, but I would like to hold my argument until I determine whether they have additional witnesses or evidence.

Mr. Burke: Well, their statement is about as clear as their motion, so I will then proceed to move to dismiss denying their motion to dismiss at this time. They have closed

their evidence and I think it would be proper to move to strike their motion to dismiss at this time.

The Court: That motion will be denied.

Mr. Burke: I wasn't aware I had finished my argument.

The Court: I don't care to hear any argument along that line Mr. Burke. If the debtor has any evidence to offer, I will be happy to hear it.

Mr. Burke: The debtor would call Mr. I. H. Peters as its first witness.

The Court: Mr. Peters will you come forward?

You were sworn previously in this matter with respect to this motion. Do you understand that that oath is still binding on you, Mr. Peters?

Mr. Peters: Yes, sir.

I. H. PETERS

was called as a witness by the debtor, and having been previously sworn, was examined and testified as follows:

155 Direct Examination

By Mr. Burke:

Q. Mr. Peters, you previously stated that you are vice-president of American Trailers Rentals Company, the debtor in this arrangement? A. Yes, that is true.

Q. When did you become vice-president, Mr. Peters? A. In the Summer of 1960.

Q. You stated on examination by the attorney for the Security and Exchange Commission, that a great many of the trailers that are in American Trailer Rentals Company were manufactured by a company known as DeMar, Inc., of Alliance, Ohio. Do you recall making that statement? A. Yes.

Q. And you also stated under examination of the Security and Exchange Commission that you aided DeMar in obtaining contract for the manufacture of these trailers. Do you recall that statement? A. Yes, I do.

Q. You also stated that you were associated with American Trailer Rentals Company at the time you obtained or assisted DeMar in obtaining this contract for manufacture.

What was your association with American Trailer 156 Rentals Company at that time? A. I was a stock-

holder, and I believe I was shown on the board of directors of American Trailer Rentals Company.

Q. When was this contract first obtained with DeMar, Inc? When were the trailers manufactured by DeMar? A. In May of 1959.

Q. What was your association with American Trailer Rentals Company at that time? A. I was a stockholder. I was shown on some of the literature of the corporation. It was printed without my knowledge or without my consent and without any knowledge of me being a director. I was not aware of this. This was arrived at through no board meeting or anything.

Q. How many shares did you own in American Trailer Rentals Company? A. Twenty-five hundred.

Q. How many shares were outstanding at that time? A. One-hundred thousand shares.

Q. Mr. Peters, at the time that American Trailers first started purchasing trailers from DeMar, who was doing the manufacturing at that time—prior to that time? A. Prior to that time, it was Selma Trailer Manufacturing Company in Selma, California and Kruger Iron Works in Meridian, Texas.

Q. Do you know the comparable cost of the trailers
157 that were manufactured as compared with the cost of the trailers manufactured by DeMar of Alliance?

A. Do I know the comparable cost?

Q. Yes. A. Generally I do.

Q. And do these costs to American Trailer Rentals Company compare? A. On certain ones or two certain models, Kruger Iron Works offered a better price than the other two corporations. Then on certain models and certain sizes of trailers, Selma had a more attractive price than either DeMar or Kruger. The whole average as it came out, I would say that every one of the manufacturers for a group of various sizes of trailers, would probably average out about the same. We were confronted with the geographical problem as well.

Q. What was this geographical problem? A. It cost money to deliver trailers from California to the midwest. It cost more to ship trailers from Alliance to the west coast.

Q. Was it desirable to have trailers in Chicago? A. It is desirable to have trailers in Chicago and undesirable to have too many trailers in California.

Q. What is the authorized capital of American
158 Trailer Rentals Company? A. Presently?

Q. Yes. A. Six-hundred thousand shares.

Q. What type stock is it? A. It is all common.

Q. How many bonds or debentures authorized are outstanding? A: None.

Q. How many shares are issued? A. Something over five-hundred thousand. I think five-hundred thirty-five thousand shares.

Q. Do you know David W. Adams? Did you know him? A. Yes, I did know him. He is now deceased.

Q. Do you know approximately when he left the—let me ask you this first: What was his association with American Trailer Rentals Company? A. Why I would say he was one of the major organizers and promoters of the company.

Q. Do you know when he left the promotion of the company? A. I believe it was in October or November of 1959.

Q. Prior to that time had you actively participated in management of the American Trailer Rentals Company?

A. No, I had not.

159 Q. When did you actively commence to participate? A. July 6, 1960.

Q. Who is the president of the company at the present time? A. James H. Dailey.

Q. When did he commence active participation in the management of the company? A. I would say at the same time I did. He became the president of the company at that time and took an active roll in the board of directors.

Q. What was the condition of American Trailer Rentals Company when you commenced your active participation in management? A. Well, at that time, American Trailer Rentals Company had under lease, maybe five hundred trailers. I don't remember exactly. Maybe seven hundred, but it was less than a thousand. These trailers were not earning the revenue that we needed for the company, and we needed more trailers to have a uniform growth, and the company for these reasons was deplorable, and it was in serious condition.

Q. I believe you testified on a question by the Security and Exchange Commission, that there were funds for which an accounting could not be made, is that correct? A. That is correct.

160 Q. When were these funds received and expended? Was this prior to your commencing an active participation

or after you became active? A. Prior to and I believe it was in the year 1959 sometime. I don't know exactly.

Q. Would it be correct to say that certain monies were received for the purchase of trailers and there were not trailers purchased? A. That is exactly right.

Q. Since the present board of directors have commenced the control of the management of the company, have any trailers purchased monies been used for any purpose other than the purchase of trailers? A. No.

Q. For all the trailers for which the company received money, were not manufactured, is that correct? A. Say that again?

Q. All of the trailers for which the company received money, were not manufactured, is that correct? A. That is correct.

Q. Where did that money for the purpose of those trailers go? What happened to that money? A. I am confused by your question. Are you speaking of the money that was received for the purchase of trailers prior to?

Q. No, after you and the present board of directors commenced active management. A. We had an arrangement with the DeMar Company where some of the money would be placed in escrow for the purchase of trailers and some of the money would be paid with the order to DeMar for the manufacture of the trailers. All of these trailers were not manufactured.

Q. Was all of the money placed in escrow? A. All of the money was delivered to DeMar or placed in their escrow account. Those trailers were not delivered.

Q. Under examination by the Security and Exchange Commission, you several time alluded to an investigation or investigations by the Security and Exchange Commission. What was the date of the first investigation to which you referred? A. I believe it was April 12, 1961.

Q. With whom did you communicate with on April 12 in the Security and Exchange Commission? A. The name of the man?

Q. Yes. A. The S.E.C. man?

Q. Yes. A. This was Gerald Boltz, an attorney.

Q. An attorney for the S.E.C.? A. Yes.

Q. Did you have any meetings subsequent to April 12, 1961 with Mr. Boltz? A. Yes, we met with him in his

office and he and a couple of other gentlemen were from the S.E.C. were in our office and there wasn't a great deal of formality in these meetings. We were accomplishing the purpose for which the S.E.C. wished us to accomplish.

Q. Did Mr. Boltz or any other person from the Security and Exchange Commission at that time make any comments concerning the management of the present management or the management at that time of American Trailer Rentals Company? A. It was a long time within two or three months from the beginning of this investigation to the end, Mr. Boltz came into our office to pick up some records, and which we freely give him, and they weren't subpoenaed. At this time, he had a great deal of background on the problems that this company was plagued with. And then at the time the S.E.C. entered into the picture, our whole appearance of our corporation activity rental structure and everything had completely changed, and Mr. Boltz commended the management of the company very highly for accomplishing this. I don't remember his exact words. It was a slang expression indicating that it was a worthy accomplishment.

163 Q. Now, Mr. Peters, would you explain briefly how this trailer-American Trailer-Rentals System operates, starting with your station operators up to the company, that is, how the trailers physically move and what is done with records and that sort of thing? A. Just the mechanics?

Q. Go ahead. A. Just the mechanics of the rental operation?

Q. Yes. A. We have authorized dealers with whom we have an agreement to rent our trailers to the motoring public or to somebody who needs a trailer to haul something. These trailers in general are located at gasoline stations spread out across the country. We have a sending station and with a receiving station with each rental agreement. At the time the person rents the trailer, say in Denver, and wishes to go to Los Angeles, the agreement is drawn between the renter and our agent in Denver. It sets forth the number of days he has to make this trip and the exact location address of our dealer which will be the receiving station to where this trailer is supposed to be delivered. The contract also includes the amount of money for the

rental and the rates. The rental is determined by concentric zones established on a map around the point of origin.

There is a map for each locality. When the trailer 164 gets to its destination, the receiving station then accepts the trailer, and at that time he mails an arrival notice to our office in Denver so that our records may indicate that that trailer has been received at this station and available for rental again, and particularly that this trailer has not been lost or stolen, and that the person that rented the trailer has lived up to his end of the contract. At the time the trailer is rented, and also as an additional safeguard, a copy of the rental contract is mailed ahead to the receiving station that is shown on the rental contract, so that this receiving station will know the trailer is coming, then this completes the phase of rental.

In our office, however, we have a trailer activity card for each trailer, and all of our stations are identified by code numbers for expediency and posting, and the movement of each trailer is posted on its' trailer activity card, included from one station to another. In handling the rentals of this nature, the service station or the trailer renting agents receive a commission, a percentage of the rentals on cross country rentals. As I have just described, it is thirty percent of the gross on that. On local rentals when an individual rents a trailer to move his furniture from one location within his own town to another, and the trailer will be returned to the same station, this is what we call a local rental. The station operator gets 165 forty percent of the gross of the rental on that.

Q. The activity cards are kept in your office? A. Yes, they are.

Q. By the personnel of the company? A. Yes.

Q. Has the trailer company received any income from the rental of these trailers? I don't mean net income, I mean gross income? A. Yes, we have received gross income from the rental of the trailers.

Q. Has that gross income in the past be sufficient to pay the administrative cost of the company? A. What does the administrative cost include? What do you mean?

Q. Your office personnel, the trailer operator; that is, the station operator? A. Some months we have enough income to pay these expenses, and some month we haven't.

Q. On the aggregate over a period of time, have you had sufficient income—gross income to pay your office expenses and the expense of running the trailers? A. Well, yes, it is just the expense of running the trailers and operating this company. We have had so many peripheral expenses that involve a great deal of expense for accounting 166 and lawyers and court costs. From April 12, 1961, our expenses have absolutely doubled because of the other expenses incurred. We have distraction of our personnel from their work. Well, we have got some of our trailer people in this room now who are definitely interested in this thing. We ought to be at work.

Q. Now, has the operation of the system—has the income from the operation of the system been sufficient to pay trailer owners the two and half and three percent contracts?

A. No.

Q. Have trailers been withdrawn from the system? A. Yes.

Q. By trailer owners? A. Yes, many trailer owners are withdrawing their trailers from the system.

Q. And have they in the past? A. Yes, they have in the past. They weren't withdrawing trailers from the system when the system was in a growth condition.

Q. Who provides the trailer owners with the information as to the location of it when they withdraw? A. American's office here in Denver.

Q. How are you able to provide a trailer owner with information as to the location of his trailer today as 167 against what it was two weeks ago? A. Well, we just refer to that activity card of that trailer.

Q. And the personnel of the company keep the activity cards? A. Yes.

Q. Now, one time you stated that W. N. Marx, president of DeMar, Inc., held approximately some 141,250 proxies on the common stock of American Trailer Rentals Company. Does he hold these proxies today? A. I do not believe so, but I am not certain. There is a little doubt in my mind, I don't know.

Q. Were you present when his attorneys advised him to release the proxies? A. Yes.

Q. Is Mr. W. N. Marx a director of this company? A. No.

Q. When did you disassociate yourself from DeMar? A. In the Summer of 1961 approximately. I don't know how you mean, disassociate?

Q. When did you stop actively participating in the management of DeMar? Did you ever have an active part? A. No, I never had an active part. I appeared on their board of directors, but I was just on the board and attended very few board meetings, and I wasn't asked many questions 168 and I didn't offer much advise as a board member.

Q. What has been happening to the income of American Trailer Rentals Company in the last two or three months? A. It has been decreasing.

Q. Are you coming into a better rental season? A. Yes, the Spring has shown an upturn in our revenue. It is a very seasonable business, however, we have never had a month where we didn't have income from trailers. Climatic conditions affect the rental of the trailers, but generally Spring is a good rental season and it reaches its peak about June.

Q. You expect the income of the company to increase in the next two months? A. That is a difficult question to answer. We have had quite a number of trailers removed from the system, and its slacked off some now. If we are successful in our arrangement, I think that our income per trailer in the next few months is going to increase substantially, but we can't increase it if these people are removing their trailers.

Mr. Burke: That concludes our questioning of Mr. Peters for the moment.

The Court: Mr. Scheid, do you have any questions of this witness. I take it this would be cross examination.

169 Q. Mr. Scheid: Yes, I have a few questions, Your Honor.

Cross Examination

By Mr. Scheid:

Q. You have stated that you were not associated with the debtor at the time—strike that.

You said you were associated with the debtor at the time that DeMar entered into a contract with the debtor

for the production of trailers, is that correct? A. Well, yes, it was an association there.

Q. You stated that you came with the debtor in the Summer of 1960? A. In management capacity.

Q. Were you with the Executive Sales prior to the Summer of 1960? A. No. What do you mean with Executive Sales?

Q. Were you associated in anyway with Executive Sales? A. You mean as a director or stockholder?

Q. Director or stockholder? A. No, I was never a director or a stockholder.

Q. An officers? A. I was shown as an officer of Executive Sales at one time, but I believe that was changed, and this occurred I believe sometime in 1960.

170 Q. Before the Summer of 1960? A. After.

Q. Did you have any contracts or anyone of your corporation have a contract with Executive Sales prior to the Summer 1960? A. I can't recall exactly. I don't believe we ever had a contract with Executive Sales. Which of the corporations do you refer to? I. H. Peters?

Q. I. H. Peters. A. I don't believe we ever had a written contract, and this may have been just an oversight, but I don't believe I have ever seen one.

Q. Did you have an oral agreement with them for the sale of trailers. A. We were selling trailers for them and it was pretty obvious we had some kind of agreement.

Q. You were selling trailers for them? Who is them? A. Executive Sales.

Q. This is prior to the Summer of 1960? A. Yes.

Q. Did this arrangement start early in 1959 or late 1958? A. It started to some extent in 1959.

Q. January or February? A. It was later than 171 this, maybe March. It is awfully hard for me to answer that, because we didn't have an agreement—a contract with them. I did sell trailers for them, and in 1959 I was the principal one that was selling trailers for them, and I wasn't working very hard at it or fulltime. I had other things. I was doing other things, and occasionally I would sell some trailers. I was interested in American Trailer Rentals Company because I had bought stock in American, and above and beyond that, I hadn't much time to participate in American. I was just simply a stockholder.

Q. Prior to this date in the Summer of 1960 when you became vice president of the debtor, were you associated with any of the state trailer rental companies that you have enumerated here? A. Prior to July 6, 1960?

Q. Yes. A. Oh yes, I was associated with Nebraska Trailer Rentals Company at that time, and this was—hadn't been in existence too long.

Q. You have testified that condition of the debtor at the time you came with the company directly was deplorable. Has that situation ever changed? A. Yes, it did change considerable.

Q. In what way. A. Well, when I come to work 172 for the company, it was at the request of other stockholders in the corporation, and it was also at the request of DeMar, and they were interested in getting trailers made that had been paid for by private individuals, and these trailers had never been manufactured and delivered into the system, and it was a very serious thing.

Through my work with DeMar, we arranged to have a manufacturing program to cover these trailers, which there was no funds to pay a manufacturer. This was a pretty serious thing. Here we either owed some people some trailers or owed them quite a few dollars, and we arranged to get the trailers manufactured and then we had a repayment program put into effect, and deplorable is an accurate word I think, and improvement is also to be recognized, because by early part of 1961, we had over five thousand trailers, and in about six or eight months, we managed to get over four thousand additional trailers into this system, and we thought that was quite an accomplishment. Our competition thought that was quite an accomplishment, and we have records to indicate that other major contenders in this industry recognized that as an accomplishment.

Q. Do you know whether prior to the date you came with the company, which I believe is July 6, 1960, the company ever had a net profit? A. No, the company never expected to have a net profit until they had enough trailers in the system to have a balance across the nation.

173 Q. From the date you came with the company, and until you had your first conversation with the representative of the Commission in April of 1961, did the corporation have a net profit? A. No, the company never did.

Q. The sale of these trailers merely resulted in an increase in the debtors fixed obligations, did it not? A. Everytime we sold a trailer, we entered a lease agreement with that trailer owner to pay him so many dollars a month based on the purchase price of that trailer. Naturally this would increase our obligations, but at the same time, it intended to increase our earning capacity to offset that obligation.

Q. I believe that you testified that the earning capacity never came up to your fixed obligations, isn't that true? A. That is true.

Q. And did you anticipate that you could sell trailers for several years and increase your fixed obligations and somehow pay them off? A. May I explain what our exact plan was on that?

Q. Yes. A. The minutes of our corporation, and if you will talk to any of the board members, present or former board members, even the people that promoted this company, it was recognized that these fixed agreements were dangerous and expensive, and would be heavy, but it was

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also recognized that to get this company growing rapidly, they would take in approximately five thousand trailers on guaranteed contracts and they would take in another four thousand on a lesser guaranteed contract and a large volume of approximately thirty thousand trailers participating in the lease agreement. That is presently being used by Nationwide and U-Haul, National. The trailer owner receives a fixed percentage of the actual rentals of the trailers, so if the trailer doesn't rent, then there is this obligation on the trailer. We were anticipating not more than nine thousand trailers on any kind of guarantee. Four thousand of that nine thousand on a reduced guarantee and thirty thousand on the open participating contract, thus giving us a cushion through this large volume of the later type of contract covering trailers and enough cushion to stand these guaranteed commitments.

Now, we were also aware that a participating contract might be a security violation, but I didn't think in the world that a fixed contract where I rent you my car for so many dollars a month is a security violation, and this was another reason for sticking with the fixed contracts to some degree.

Q. Did you make any effort to sell any of the lesser percentage contracts? A. No, we had the program. We had a meeting on St. Patrick's day; March 17, 1961.

175 Our sales were going so well, that we anticipating having too many trailers on the two percent contract and we thought—we called this meeting and rented a large room downtown at a hotel and had all of our sales representatives and all our stockholders, all of the management personnel of the corporation, and we had a two day meeting. The purpose of this meeting was to advise everybody concerned and interested in the company, both financially and that we were discontinuing this two percent—the offering of this two percent contract, because we had all that our program could absorb. We discussed the lesser contract and how it would be sold and when it would commence and so on.

Q. Did you ever attempt to sell any other fixed percentage contracts? A. The previous management had those contracts available, and some were sold. I don't believe there were any sold after July 6, 1960. I can't guarantee that statement. To my knowledge, they weren't.

Q. Do you have any knowledge as to whether the sale of such contracts—the thirty-five percent rental contracts, was more difficult than the fixed percentage rental contract? A. Well, I believe it would be more difficult, however, prior to my coming to the company, several people who sold these, National, Nationwide, had been selling them too.

176 Other competitive systems have been selling them very successfully and without registration.

Q. Incidentally, how many trailers did you personally receive sales commissions on? A. How many what?

Q. How many trailers did you personally receive sales commissions on? A. I couldn't answer that. I, myself as an individual or my corporation or what?

Q. Received them directly or indirectly? A. I have no idea. I have sold a sizable number of trailers, but I don't know how many. That is pretty tough, Mr. Scheid. I will calculate it for you if it is important.

Q. Is it your testimony that after you came with the company, that most of the trailers were sold, isn't that correct? A. After I came to the company, most of the trailers were sold.

Q. Have you stated that there were five hundred trailers when you became vice president? A. Let's say there were something less than one thousand trailers.

Q. And since that time, more than five thousand trailers were sold and I wondered how many of those were sold through your efforts.

177 Q. Mr. Burke: That doesn't correctly state the witnesses previous testimony.

(The Court: I don't think that is necessary.)

Mr. Burke: I wanted to point out a misleading portion. He said since that time, five thousand trailers were sold, and I think Mr. Peter's previous testimony was five thousand trailers were sold as a whole. I don't think that you intended that.

Mr. Scheid: I believe the record will show that they had five thousand eight hundred sixty-six trailers, so I originally took the original five hundred and called it eight sixty-six and evened it off at five thousand.

The Court: I think that is a fair assumption Mr. Burke, based on that assumption. Go ahead with your questioning, Mr. Scheid.

Q. How many of these trailers did you sell personally after you became vice president? A. After I became vice president! Now, did I sell personally? In other words, I know a fellow down the street and I go and sell him a trailer. Is this what we are talking about?

Q. Yes. A. Well, maybe I might have sold one hundred. I don't know.

Q. How many persons employed by you sell? A. 178 Employed by L. H. Peters Company?

Q. By you in any capacity? A. Well, there were people employed by me when I was the management head of the American Trailer Rentals Company.

Q. Let's limit it to any other company. A. Other than American or Executive Sales?

Q. Other than American. A. Well, I had some knowledge and direction in quite a bit of this program. I wasn't called the sales supervisor or sales superintendent. Each state had its own selling organization, and they managed their own sales within their own states.

Q. You say you were primarily responsible for these sales? A. Well, does primary responsibility mean I was the only one responsible for these sales?

Q. I will withdraw the question and ask it a different way. Did you or any corporation controlled by you or any organization under your control receive commissions on the majority of the trailers sold after you became vice president of the debtor? A. Well, let me try to answer it this way, Mr. Scheid. L. H. Peter's Company sold trailers.

I. H. Peters had salesmen.

179. The Court: Let's have the question read, and I want you to answer, and I think it is proper for you to answer it.

(Last question read by reporter.)

A. Well, yes, it would be yes.

Q. Thank you. A. It is difficult for me to know which corporation or how you mean control and authority.

Q. You have stated that Mr. Marx is not a director of the debtor. Was he a director of the debtor? A. Yes, he was.

Q. When did he resign? A. I can't be certain. It was either the later part of '61 or early '62.

Q. Did Mr. Marx come on the board of directors of the debtor at the same time you did? A. Yes.

Q. Was that pursuant to an agreement with you? A. No.

Q. Did you have any agreement with—about seating Mr. Marx on the board with any person? A. Not to my recollection.

Mr. Scheid: I have no further questions Your Honor.

180. The Court: May I see Exhibit "E"? We will be in recess until 11:00 o'clock. Then with permission of counsel, I am going to take the exhibit back to chambers and read it.

Thereupon a recess was taken at 10:50 a.m.

The Court: Off the record.

Thereupon a discussion was had off the record between the Court and counsel for the respective parties.

The Court: Mr. Burke, do you have any further questions?

Mr. Burke: Yes, Your Honor, I have a few more questions.

Redirect Examination

By Mr. Burke:

Q. Mr. Peters, the Court advised you should answer a question as to whether you received any interest in the majority of the sales commissions, and if you wanted to explain it, your attorney would give you the opportunity. I now ask you what happened to these sales commissions. Did you have any interest in them? A. Well, the majority of the sales commissions, I didn't have any personal gain in them. Now, whether I wanted to or not, I worked with Executive Sales. I didn't want to very badly, but I had to, because the sales had to be correlated with the leases

and the posting, and I being familiar with the sales, 181 I worked with Executive Sales in that capacity that

I just described. So Executive Sales had an override on these trailers, on the sale of them and it went to this company. And this was actually loaned to American Trailer Rentals, some of this money from some of this override to offset delivery of trailers in the system, like our original insurance on the trailers or original book-keeping setup, and this was used generally for this purpose. Now, that is the extent of it and that was a pretty hard question to answer yes or no.

Q. Now, in regards to L. H. Peters, did L. H. Peters receive commissions on trailers sold by anyone else? A. None other than sold by L. H. Peters Company.

Q. And in relation to the total number of trailers sold, how many did L. H. Peters sell? A. The percentage would be very small. Actually I couldn't quote the percentage or the exact number of trailers L. H. Peter's Company sold. L. H. Peter's Company might have sold in all, three hundred trailers. It has been tabulated months ago; and I have completely forgotten what it was.

Q. Were you actively running L. H. Peters Company during the main portion of this time? A. No, L. H. Peters was a corporation and another stockholder and director in the corporation as actively running L. H. Peters, Company at all times since I have been in any management capacity with the American Trailer Rentals Company.

182 Q. What were you doing there at this time? A. I was managing American Trailers Rentals Company.

Q. Fulltime? A. Yes.

Q. At the time you became actively engaged in the management of American Trailer Rentals Company, were you engaged in any other businesses? A. Yes.

Q. What were these businesses? A. General Contracting and engineering business. I was also farming.

Q. When did you discontinue those activities? A. About the time I went to work for American Trailer Rentals Company. I had to discontinue contracting. It was a business that I had built up myself and through bidding and estimating and so on on every project, and it was generally conducted by myself and I didn't have time to do this. My farming was limited to wheat farming, which is a fairly simple operation with mechanization as it is today, and I had a hired man that I turned this over to and it didn't take a great deal of my time. I could handle that on weekends.

Q. During the year 1960, who was managing the Executive Sales Company? A. During the entire year of 1960?

183 Q. No. A. Up to July 6, 1960, Richard J. Rutherford was managing director of Executive Sales Company.

Q. Now, you stated that in March of 1961, there was a meeting held in which you discussed the reduction of the fixed percentage contracts to a lower figure, and you also stated that that figure was never reached, that is, you never sold any trailers. When did that figure go into effect? A. May 1, 1961.

Mr. Burke: That is all.

The Court: Mr. Peters, will you refresh my memory again. When did you become executive vice president of the debtor? A. July 6, 1960.

The Court: Was there a general change in management of the debtor at that time? A. Yes.

The Court: Was there a new board elected? A. Yes, there was.

The Court: Was it entirely new or partial? A. Partially new.

The Court: Of the old directors, who were retained?
A. May I explain how the old director arrived at
184 being a director. I was called a director on the old
board. There was never a stockholder's meeting
which affirmed this selection of me as a director. After
July 6, we called a stockholder's meeting and elected the
directors properly. Now, I remained on the board and
James H. Dailey remained on the board, who was shown
on the previous board. R. J. Rutherford went off the board.
Joseph L. Flores appeared as vice president and general
manager on the old board. He continued in this position.
Joseph L. Flores is still in management capacity of the
company and is very satisfactory. Really the people who
went off the board were those who promoted the company.

The Court: That was Rutherford and whom else? A.
And Jack Grible.

The Court: Where does Adams fit into this picture?
A. Well, Adams was disposed of by Rutherford and Grible
prior to my arrival on the scene, and I believe it was about
two months after I was in a management capacity that
Mr. Adams died.

The Court: Do you have any opinion as to whether or
not there was any misconduct on the part of management
prior to July 6, 1960? A. Do I have any knowledge of
it?

185 The Court: Do you have an opinion? A. Yes, I
certainly do have an opinion.

The Court: What is that opinion? That there was or
was not mismanagement? A. There was.

The Court: I would like you to identify the people,
though. A. I attributed it almost completely to Mr.
Adams, who is a tremendous man, but he didn't handle
money right.

The Court: When did he die? A. I believe it was about
October of 1960 as I recall.

The Court: Did he leave any estate? A. No, I believe
he died penniless.

The Court: Has there ever been any effort on the part
of management since July 6, 1960 to explore the possi-
bility of recovery of anything from this former manage-
ment? A. Yes, there has been, and have been advised
that it would be a nice moral victory, but probably nothing
more.

The Court: Advised by whom? A. Our counsel, and we have discussed this with our accountant too.

The Court: Now, I take it that counsel advised you whether or not you had a cause of action. You wouldn't go to counsel to find out whether a judgment was collectible or not, after it was obtained, would you, Mr. Peters?

186 A. No.

The Court: If you knew it was a bad financial risk, you wouldn't go ask your lawyers, would you? A. No, we were aware of the financial situation of the people whom we would have to get a judgment against.

The Court: All right, name the persons that you think would be liable for the judgments; not to payment of them necessarily, but to judgments? A. Well, my primary or our original thinking was Mr. Adams, but we had just started talking with him when Mr. Adams died. And he really maintained complete control of that thing when he was running it. There was nobody else made a decision, and it was Rutherford who found himself involved with Adams and being a participant in these things and unknowingly he was implicated for things Adams was doing. Rutherford was trying to protect himself by getting rid of Adams. He attempted to clean this thing up. He wasn't successful.

The Court: In other words, you don't know any living person that could be proceeded against, is that right? A. Well, I don't really know, Your Honor. I don't want to make any accusations under oath that aren't really founded, and I don't think I am qualified to make this judgment against these two remaining people who are alive.

187 The Court: How many stockholders are there in A.T.R.? A. It is approximately one hundred I believe.

The Court: And does any one group control the corporation? A. No, sir.

The Court: For example, how many shares do you have, Mr. Peters? A. I have 32,500 shares.

The Court: And who is the largest single stockholder? A. Well, I think Dailey and Rutherford have about the same amount of stock. I think each of them have something like 70,000 shares.

The Court: Now, why would it not be in the best interest

of the corporation and stockholders to endeavor to proceed against those responsible for the improper disposition of its fund prior to July 6, 1960? A. Well, I believe it would be proper, but it has been my opinion to actually prove anything, it would be against Adams himself and Adams went out without any stock, and his estate contained no assets.

The Court: Now, how much stock does Mr. Flores own?

A. He owns 10,000 shares.

188 The Court: What connection did he have with the Adam's transactions? A. Well, Mr. Flores was strictly operations. His responsibilities were in operating the trailers after they were in the system. He did not participate in sales, finance, promotion, selling of stock. His was purely operational, and he was completely disassociated with these people—this group of organizers, they didn't think alike, and their duties were so divorced between the two groups, that Flores had no participation in this promotion of the company.

The Court: Did you ever arrive at the conclusion as executive vice president and director of the debtor as to how much in terms of dollars Mr. Adams owed the company? A. I believe it was trailers that weren't manufactured. I believe it was \$141,000.

The Court: Is that the extent of Adams' liability in your opinion? A. It could be more. That is the only thing that I can state definitely, that I would really know that was missing.

The Court: What device did Mr. Adams use to remove the \$141,000 from the company? A. How was it accomplished?

189 The Court: Yes. A. Well, I have learned some of this by hearsay. This statement may not be completely accurate, but money came into Executive Sales when the trailer was sold and Executive Sales was to pay this money to the manufacturer for that trailer. Well, Mr. Adams was, I believe, the president of Executive Sales at that time and so the money didn't go to a manufacturer. Mr. Adams could take this money and could do anything he wanted. He had authority to sign checks for Executive Sales Company, and it just took his signature only, and he could and did anything he wanted to with this money.

The Court: All right, then did he take the money from A.T.R. or from Executive Sales in your opinion? A. Well, actually you can't pinpoint it. It was taken from A.T.R., but indirectly it was taken from A.T.R.'s portion of it because the commitments for the lease payments to these trailer owners for which trailers didn't exist was still paid to the trailer owners by A.T.R., so in effect, Adams was taking away the earning capacity for which A.T.R. was obligated to make payment.

The Court: In your testimony, you talk about escrow payments, monies that were to be kept in escrow for the benefit of DeMar as I understood it, is that correct?

190. A. Well, not for the benefit of the manufacturer of trailers. Approximately half of this money that came from the sales of trailers from individuals, this money was placed with Executive Sales, and they were entrusted to have trailers manufactured with this money. Now, Executive Sales placed half of this money in escrow, and the escrow agreement provided that the money would be paid to the manufacturer upon the completion of the trailers and the delivery of a title, or either a certificate of origin. The certificate of origin is similar to an automobile certificate of origin for licensing purposes and this is the document which—when taken to the escrow agent, then the money was released.

The Court: Did DeMar get the money that was put in escrow? A. You bet. Yes, sir, they made trailers for that money.

The Court: But DeMar now asserts a claim against A.T.R. roughly \$190,000, as I recall. Is that correct? A. Well, the claim I seen was for \$90,000.

The Court: Is that amount due from A.T.R. in your opinion, or from Executive Sales to DeMar? A. Executive Sales and A.T.R. have since merged, so it would be due, if this were owing, and no offsets against it, then this amount would be owing by the surviving corporation, which is A.T.R.

191. The Court: Then that brings up the question, when was the merger between Executive Sales and A.T.R.? A. It was some time in 1961. These corporations were merged for the purpose of filing our registration with the S.E.C.

The Court: And you were aware of these transactions between A.T.R. and Executive Sales and DeMar when you voted for the merger, weren't you? A. Yes, sir.

The Court: The effect of the merger was to unload a great deal of liability on A.T.R., which therefore belonged exclusively to Executive Sales! A. Not exactly. We felt in registering, we were going to have a continuing sales program. Executive Sales had this overriding arrangement on sales and it was in an agreement. Some of the directors and owners of Executive Sales were not acting in the interest of A.T.R. In other words, here were cousin corporations, but one cousin wasn't being very friendly, and certain persons who controlled Executive Sales were—had themselves set up to make a fortune off of the sales, and A.T.R. wasn't going to get anything out of it except Executive Sales would lend A.T.R. money as they needed it, and eventually it would have ended up that Executive Sales would have owned A.T.R. and our only solution at that time was to eliminate that drain of funds into

192 Executive Sales, and the need of A.T.R. was to have a statutory merger.

The Court: After the merger, how much of A.T.R. funds were used to discharge obligations of Executive Sales? A. I don't believe you mean the surviving corporation then?

The Court: Yes. Executive Sales came into the merger with substantial debts, did it not? A. Well, Executive Sales had substantial debts, and A.T.R. owed Executive Sales a lot of money by the same token. As I recall, it was kind of a balancing operation. Now, the amount they paid off, I don't recall, but essentially it was through the manufacturing agreement with DeMar that was the main debt, and this was being reduced. It still was never completely reduced. I would guess about sixty or seventy thousand dollars of this debt to DeMar was paid by A.T.R. following the merger.

The Court: Well, you voted for the merger. What in your opinion was the advantage to A.T.R. to be derived from the merger? A. Well, Executive Sales had an arrangement where they would have exclusive sales rights for all trailers going into American Trailer Rentals system, and this was a written agreement, and the people of

Executive Sales would not reduce this, and it was
193 increasing the lease obligations to A.T.R., and by
the same token, Executive Sales was lending money
to A.T.R. which would eventually give them control of
A.T.R. This we didn't want, and we felt it was better
to merge, so the surviving corporation would have the
overriding benefit of this sales, as I recently discussed
under examination. It took a little money to deliver the
trailers and license the trailers and buy the insurance, and
this was the only source we could find for it. We weren't
going to have an economical operation until we had eight
or ten thousand trailers in the system.

The Court: As of July 6, 1960, how much identical
management between A.T.R. and Executive Sales? A. As
I recall, the management of A.T.R. did not change after
the merger.

The Court: No, were there any as of July 6, 1960 when
you became executive vice president of A.T.R., how many
officers and directors of A.T.R. were officers or directors
of Executive Sales? A. I believe only one.

The Court: And that one was who? A. And that was
Mr. Dailey.

The Court: Now, at the time of the merger in 1960, did
A.T.R. explore any avenues for escaping from these con-
tracts, which Executive had, other than the merger?

194 A. No, we did explore them, but it didn't seem
feasible at the time.

The Court: Did you take the advice of counsel? A. Yes,
sir.

The Court: Who were the attorneys involved? A. Well,
Mr. Burke and I believe Mr. Maxwell was consulting with
us at that time—yes, it was both Mr. Burke and Mr.
Maxwell.

The Court: Were there any other counsel involved with
those gentlemen at that time? A. Yes. It wasn't our
attorney, but there was—I am confused, these were the
only two lawyers.

The Court: Did Executive Sales have counsel? A. Mr.
Burke was Executive's counsel.

The Court: And also counsel for American Trailer
Rentals Company? A. Yes, sir.

The Court: Mr. Maxwell was also in a dual capacity?
A. No, he was counsel for American.

The Court: Any further questions, gentlemen?

Mr. Scheid: None, Your Honor.

195 Mr. Burke: I have one question in regard to your inquiry.

Further Direct Examination

By Mr. Burke:

Q. It may evolve into three.

The Court: I am not going to limit you.

Q. Mr. Peters, you stated that there was a debt from American Sales that A.T.R. owed Executive Sales at this time? A. Yes.

Q. This was on loans—cash loans made by Executive to American? A. Yes.

Q. Do you know the amount of that debt at that time? A. No, I don't, but it was, I believe eighty or ninety thousand dollars.

Q. Now, in regard to this claim of DeMar, what is your opinion as to the validity of the claim of DeMar? A. Well, A.T.R. borrowed money from DeMar, and these loans were evidenced by notes that we issued. At the same time that this was being done, we had approximately seven hundred trailers manufactured by DeMar—the largest trailers we had. I believe the price on them was around \$700 a piece. These trailers weren't usable, because they had a suspension system, due to the type of axle or the installation of the axles or the suspension of these axles, and we had to ground all these trailers

196 and change all these axles. We asked DeMar to do it, and by the same token, these trailers were all over the country at the time, and it cost us a lot of money. We calculated the amount of money it would cost us and this amount in itself was about equalled the amount that we owed DeMar on notes as I recall. Then the next thing, we got a bad bunch of tires. DeMar started putting two-ply tires on these trailers and without our knowledge, and then we had to analyze that and estimate how many two-ply tires were out, because we were starting to have quite a large amount of tire failure in the system, so we had to change a lot of tires and trace these down and stop a lot of trailers, to get these new tires on. This increased the amount that DeMar owed us then over the amount we

owed DeMar. Then at the end of the line, we paid DeMar for something like \$150,000 worth of trailers—the cash portion of our purchase agreement with DeMar. As you recall, we had half of the money put in escrow and part of it was cash with order. And the escrow for those were paid and the cash order with the trailers, and this all added to another \$140,000 or \$150,000 or something in this neighborhood. A portion of these trailers were manufactured by DeMar, went into an agreement with Mercantile Discount Corporation, which is a manufacturing firm in Chicago, with Lawrence Company, and they have offices in Denver and all over, to warehouse a portion of these trailers that had been built. These trailers had never been titled or a certificate given on these trailers, so

197 DeMar felt they were their property, and they mortgaged these trailers in this warehousing arrangement, and when DeMar went bankrupt, these trailers were then repossessed by Mercantile Corporation, and they contend these are—we contend these are our trailers, because we, with each payment, we identified the serial number to be placed on the trailer, the size of the trailer, the delivery date, the owners name and the serial numbers were on many of these trailers. We had the cancelled checks and our attached copy of the purchase order, proving that these trailers, which we had identified in the inventory, with Lawrence's permission, are the trailers we paid for. But to date, we have been unable to legally get these trailers released, so we must assume we are not going to get them.

Q. Has American Trailer Rentals Company filed a claim with the estate of DeMar? A. Yes.

Q. Does that claim exceed the amount that DeMar claims? A. Yes.

Mr. Burke: That is all.

The Court: You may step down Mr. Peters.

Any further evidence on the part of the debtor, Mr. Burke and Mr. Maxwell?

Mr. Burke: Not on this motion.

The Court: Anything further on the Security and Exchange Commission?

198 Mr. Scheid: Nothing further, Your Honor.

The Court: Off the record.

Thereupon a discussion was had off the record.

The Court: The hearing will be continued on confirmation until April 5 at 1:30 P.M.

If there is nothing further to come before the court, we will adjourn.

199 Reporter's certificate to foregoing transcript omitted in printing.

235 (File endorsement omitted)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

No. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor*.

Proceedings for an Arrangement
in Bankruptcy.

**Report and Recommendations of Benjamin C. Hilliard, Jr.,
Special Master, With Respect to Motion of Securities and
Exchange Commission to Dismiss This Proceeding Under
Section 328 of the Bankruptcy Act; With Respect to Fees
of Reporters By Whom Transcripts Were Prepared; and
With Respect to Compensation of Special Master—April
17, 1963**

To the Honorable Alfred A. Arraj, Chief Judge of the United States District Court for the District of Colorado, sitting in bankruptcy, the report of Benjamin C. Hilliard, Jr., the undersigned Special Master, respectfully shows:

I

REFERENCE, HEARINGS, NOTICES, APPEARANCES AND ISSUES

February 20, 1963, Securities and Exchange Commission (Commission) filed a motion to dismiss this Chapter XI proceeding under the provisions of Section 328 of the Bankruptcy Act. February 26 the motion was referred to Benjamin C. Hilliard, Jr., Referee in Bankruptcy, as

Special Master, to hear and report. By order of the Special Master the motion was set down for hearing, and was heard on February 26 and March 8 on notice to the debtor and the Commission. The Commission appeared by William D. Scheid and William J. Cooney, its attorneys, and the debtor by Gilbert C. Maxwell and Arthur W. Burke, Jr., its attorneys.

The issues and matters to be determined are these:

- (a) Should the motion of the Commission under Section 328 be sustained or denied? (b) May the Court, if so advised, require the Commission to pay the fees of the reporters who prepared the transcripts of the evidence adduced upon the hearing of the motion? (c) The amount and payment of compensation to be allowed the Special Master.

II

BACKGROUND

The debtor is a Colorado corporation organized September 18, 1958. Into it have been merged eight trailer rental companies formed or which engaged in business in Arizona, Colorado, Iowa, Kansas, Nebraska, North Dakota, South Dakota or Wyoming, and a sales company, Executive Sales, Inc. The interconnection of these and other corporations and the debtor, and the identity of 236 management and control of the various corporations, are explored at some length in the briefs filed by the parties. The Special Master does not feel that, upon the present state of these proceedings, it is necessary more than casually to inquire into these matters. It should be borne in mind the debtor is, by order of the Court, in possession of its business and to some extent is operating it.

It appeared from the evidence heard by the Special Master that an aggregate of \$3,590,168.00 was obtained by the debtor, and by the companies merged into it, from hundreds of persons severally living in many states, for the purchase of trailers. The salesman who sold a trailer invariably and immediately, as a part of the whole transaction, arranged a lease of the trailer to the debtor or one of its predecessors. The trailer purchasers-lessors were

entitled, under the leases, to returns varying from 2% a month for 10 years, 3% for five years, to 35% of rental income less repairs. Purchasers-lessors were advised the trailers would be placed in what was represented to be the nation-wide system of the debtor and be rented by its agents to persons desiring the use of such equipment. It was represented there would be such agents in important locations throughout the country and it appears a great many such agents had been designated by the debtor and were and are acting in varying degrees of efficiency and reliability.

The debtor had operated at a loss since its inception and there is reason to believe that "rentals" paid out by it to trailer lessors were derived in part from funds received from subsequent purchasers-lessors. At no time in the debtor's history has the rental income been sufficient to meet the aggregate of the obligations of the lease agreements. It also appeared, and the proposed arrangement recites, that some \$200,000.00 was received from purchasers-lessors for trailers never manufactured or delivered. And the schedules filed by the debtor establish that at the time of the filing of the initiatory petition—December 20, 1962—the debtor was insolvent as that term is defined in the Bankruptcy Act.

III

THE PROPOSED ARRANGEMENT

The proposed arrangement filed by the debtor was submitted to the creditors and, at the continued session of the initial meeting of creditors held on March 7, 1963, was duly accepted. In brief summary, this arrangement, after providing for rejection of the lease agreements as 237 executory contracts, and for payment of certain priority costs, expenses and debts as is required by Section 367, contains these stipulations:

1. The amounts due trailer owners-lessors (stated to be \$710,597.53) is to be paid "upon receipt of Certificates of Title to the trailers" by issuing one share of stock in Capitol Leasing Corporation "for each \$2.00 of the remaining capital investment" of an owner-lessor in his trailer, and "if Certificates of Title to all the trailers are

assigned to Capitol Leasing Corporation, a total of 766,451 shares will be issued by Capitol Leasing Corporation covering such assignments of trailer titles."

2. Capitol Leasing Corporation will issue one share of its stock "for each \$2.00 paid for trailers which were not manufactured, in the amount of \$200,677.31, or 100,388 shares."

3. General creditors, a term which as used in the arrangement includes officers, directors and stockholders of the debtor to whom it owes money; station operators (trailer rental agents); field representatives; and creditors to whom moneys are due for trailer repairs and equipment, are to receive one share of Capitol Leasing Corporation stock for each \$3.50 of debt, a total number of shares of 103,935.

4. Unsecured debts due a bank (\$40,000.00) and the debtor's accountants (\$15,577.95), are to be refinanced by Capitol Leasing Corporation and be secured by trailers owned by Capitol Leasing Corporation.

IV

SUMMARY OF THE VIEWS OF THE COMMISSION

The Commission argues that the proposed arrangement is unfair and inadequate and fails to meet the "needs to be served," citing in this regard *General Stores Corp. v. Shlensky*, 350 U.S. 462 (1956). Many grounds of inadequacy of the arrangement are suggested in the Commission's briefs. Thus it urges (1) that there is need for an overall reorganization of the debtor; (2) that there is need for investigation by an independent Chapter X trustee of the history and business affairs of the debtor; (3) that the creditors (meaning trailer purchasers-owners-lessors) are in need of the information and advice which a Chapter X trustee could make available to them under Section 167(5); and (4) that the proposed arrangement is neither fair nor equitable to the public investors (meaning trailer purchasers-owners-lessors) and is not feasible.

238 All of the reported cases dealing directly with Section 328 are cited by the Commission. They are: *General Stores Corp. v. Shlensky*, 350 U. S. 462; *Securities*

and Exchange Commission v. Wilcox-Gay Corp., 231 F. 2d 859; *Securities and Exchange Commission v. Liberty Baking Corp.*, 240 F. 2d 511; *In re Lea Fabrics, Inc.*, 272 F. 2d 769; *In re Transvision, Inc.*, 217 F. 2d 243, and *In re Herold Radio & Electronics Corp.*, 191 F. Supp. 781. The latter contains an excellent discussion of the principles involved and is the latest reported pronouncement on the subject.

V

VIEWS OF THE SPECIAL MASTER

The weakness in the position of the Commission, as the Special Master is convinced, is that at this stage of the proceeding the grounds advanced by the Commission in support of its motion are at best premature. Examination of the facts in hand and the applicable law will, it is believed, sustain this assertion.

Section 328 provides that the Court shall dismiss a proceeding under Chapter XI, but afford the debtor or creditors opportunity to amend the pending Chapter XI petition to comply with Chapter X, if the Judge "finds that the proceeding should have been brought under Chapter X." The section in effect is a codification of the rule of *Securities and Exchange Commission v. U. S. Realty and Improvement Co.*, 310 U. S. 434, and permits the exercise of the discretion of the Court within "allowable bounds." *General Stores Corp. v. Shlensky, supra.*

In considering the exercise of this discretion in the case at bar it is desirable and necessary to examine into the facts presently in the record and into the interrelation of Section 328 and Section 146(2). The latter section forbids, as lacking in good faith, an initiatory Chapter X petition which does not set up that adequate relief is unobtainable under Chapter XI. In other words, Chapter X is not available to a corporate debtor unless it establishes that Chapter XI is inadequate. How, then, may one determine the adequacy or inadequacy of Chapter XI?

In the instant case it is proper at once to reject the Commission's contention that, because the proposed arrangement provides for payment of debts through the issuance of stock of a new corporation, the arrangement

239 trespasses upon exclusively Chapter X territory. For
Section 356 of Chapter XI expressly permits
"altering the rights of unsecured creditors . . . for
any consideration," and Section 306(2) defines "consideration"
to include "stock."

The thrust of the Commission's argument is that the proposed arrangement is not feasible and is neither fair nor equitable to the public investor. These assertions may ultimately be found to be true and to be wholly or partially applicable. But at the present stage of this proceeding we ought not to consider them because if we do we deprive the Court of its right, if the facts warrant, to confirm, or to deny confirmation upon one or more of the grounds set up in Section 366. Or, otherwise stated, the Court—upon consideration at this stage of a Section 328 motion in the presence only of the Commission and the debtor—is asked by the Commission to determine facts properly to be heard and determined under Section 366 in the presence of the creditors. Nor is the Commission necessarily excluded from being heard on the subject of confirmation, for on March 22 it filed a motion to intervene which has not yet—at the request of the Commission—been brought on for determination.

The hearing on confirmation under Section 366 has been continued from time to time—it is now set for May 6—pending determination of the Section 328 motion. The Commission insists the Section 328 motion must be first decided and the Special Master has not thought it proper, in his capacity of Referee, to proceed at this time with the confirmation hearing. But the Special Master is of the view, and emphatically so, that determination of the Section 328 motion ought to be postponed to the confirmation hearing. The Special Master does not subscribe to the indirect charge of the Commission, inherent in its argument, that the Court will not give adequate consideration to determination of the petition for confirmation. To the contrary it is the belief of the Special Master the Court will not confirm unless it is satisfied the proposed arrangement is for the best interests of the creditors and is feasible, and that it is in good faith.

If the arguments of the Commission are sound the proposed arrangement is not in the best interests of the

creditors, is not feasible, lacks good faith, and its acceptance was procured by forbidden acts. Again it seems fair to assume that if all or any of these assertions are, on the confirmation hearing, found to be true, the Court will reject and not confirm.

Before this debtor is to be required to proceed under Chapter X (or as a bankrupt, or not at all) it ought first to be afforded reasonable opportunity to show that 240 Chapter XI is adequate. If Chapter XI is adequate there is no place or room for Chapter X, as Section 146(2) plainly demands. This reasonable opportunity should include the right, if confirmation is presently denied upon one or more of the grounds the Commission has detailed, or otherwise, to ask for leave to amend the arrangement to obviate those objections, as Section 363 permits. Cf. 8 Collier on Bankruptcy (14th Ed.) 1144, 1145, n.15; *In re Realty Associates Securities Corp.*, 69 F. 2d 41 (2 Cir. 1934).

In sum, the Special Master is unable to find, upon the present record, that the Commission has made a sufficient showing to warrant the granting of the Section 328 motion. For unless and until, through the processes Section 363 and 366 can afford, it has been made to appear that Chapter XI is adequate, grounds for granting the motion have not been presented.

VI

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The Special Master hereby adopts the foregoing, and respectfully submits the same, as his findings of fact and conclusions of law with respect to the issues raised by the Section 328 motion involved.

VIII

RECOMMENDATIONS

The Special Master respectfully recommends

- (1) That the Section 328 motion of the Commission be overruled, without prejudice to its renewal if and when it

has been made to appear Chapter XI is inadequate in the premises.

243 Done at Denver, in said District, this 17th day of April 1963.

Respectfully submitted,

B. C. HILLIARD, JR.
B. C. Hilliard, Jr.
Special Master.

244 CERTIFICATE OF FILING AND OF SERVICE OF COPIES
(Omitted in printing)

318 IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In Proceedings for an Arrangement
IN BANKRUPTCY No. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor*

Notice Dated January 8, 1963 of Meeting of Creditors, Etc.

To the debtor above named, its creditors and all other parties in interest:

NOTICE is hereby given that on December 20, 1962, said debtor filed a petition in this Court proposing an arrangement with its unsecured creditors under the provisions of Chapter XI of the Bankruptcy Act; and that a meeting of its creditors will be held at 10 A.M., February 1, 1963, in the Bankruptcy Court Room, Post Office Bldg., Denver Colorado, at which time and place the creditors may attend, then or theretofore prove their claims, nominate a trustee, appoint a committee of creditors, then or theretofore file written acceptances of the proposed arrangement, and transact such other business as may properly come before the meeting.

NOTICE is also hereby given that application to confirm the arrangement shall be filed on or before February 28, 1963, and that the hearing on said application and objections thereto, if any, will be held at 9 A.M., March 1, 1963, in the Bankruptcy Court Room, Post Office Bldg., Denver Colorado.

Annexed hereto is a copy of the proposed arrangement. A summary of the assets and liabilities of the debtor, as reflected by its schedules, is as follows:

Accounts receivable	\$173,196.07	Secured debts	\$ 5,611.58
Furniture and equipment	10,712.75	Executory contracts	727,585.97
Vehicles and service equipment	1,700.00	Accounts payable	230,783.29
Trailer Rental System —an intangible asset	500,000.00	Notes payable	392,533.15
		Wages and commissions	6,691.97
		Taxes	4,684.70
Total assets	\$685,608.82	Total Liabilities	\$1,367,890.66

Dated at Denver, in said District, January 8, 1963.

BENJAMIN C. HILLIARD, JR.
Chief Referee in Bankruptcy,
463 Post Office Bldg.,
Denver 2, Colorado

319

(Filed Mar. 7, 1963)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In Proceedings for an Arrangement
No. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor*.

Report of Committee

To: The Honorable Benjamin C. Hilliard, Jr.
Chief Referee in Bankruptcy

The undersigned, appointed as a Committee to examine and report the number and amount of claims filed and ac-

ceptances or rejections filed, herewith, make a definitive report with respect, thereto.

Total number of PROPER CLAIMS filed to 12:00 Noon,	
March 7, 1963	584
Total number of PROPER ACCEPTANCES filed to 12:00	
Noon, March 7, 1963	347
Total Dollar Amount of PROPER CLAIMS filed	\$1,039,020.09
Total Dollar Amount of PROPER ACCEPTANCES	
filed	\$ 580,581.77

Excluded from the above calculation are claims and acceptances as to which the Proof of Claim did not contain dollar amounts or were not properly signed.

Included in the above calculation are four (4) claims, docketed as numbers 58, 59, 60 and 67, which are calculated on the basis of the amount of back rental due and future rental due under the leasing agreement. These claims total \$42,207.59, after the deduction of rentals received by these claimants. There is a difference of opinion as to the calculation of these four (4) claims with respect to future rentals which might be due, Mr. Maxwell taking the position that future rentals should not have been computed, and the balance of the Committee taking the other position.

Each member of the Committee devoted ten (10) hours each in its services in connection with this Committee.

Respectfully submitted,

/s/ TRUMAN C. ENGELHARDT
 Truman C. Engelhardt
 2346 First National Bank
 Building
 Denver 2, Colorado

/s/ MARTIN J. ANDREW (AC 2-1471)
 Martin J. Andrew
 801 Equitable Building
 Denver, Colorado (MA 3-1245)

/s/ GILBERT C. MAXWELL
 Gilbert C. Maxwell
 2550 First National Bank
 Building
 Denver 2, Colorado
 (AM 6-3558)

140

320

(Filed Mar. 7, 1963)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In Proceedings for an Arrangement
No. 33276

In the Matter of
AMERICAN TRAILER RENTALS COMPANY, *Debtor*.

Application for Confirmation of Arrangement

To: Honorable Benjamin C. Hilliard, Jr.
Chief Referee in Bankruptcy

American Trailer Rentals Company, a Colorado corporation, the above named Debtor, respectfully represents:

1. The Arrangement under Chapter XI of the Act of Congress relating to Bankruptcy proposed in the Petition filed by the Debtor on the 20th day of December, 1962, has been duly accepted in accordance with the provisions of said Chapter.

2. The consideration consisting of shares of no par value common stock of Capitol Leasing Corporation, a Colorado corporation, is subject to the approval of the majority of the shareholders of Capitol Leasing Corporation, and said shareholders meeting will be promptly called and held and the shares will be deposited with the Court, subject to the Order of the Court herein.

3. The provisions of Chapter XI of said Act have been complied with.

4. Said Arrangement is for the best interests of creditors.

5. Said Arrangement is feasible.

6. The Debtor has not been guilty of any of the acts, or failed to perform any of the duties which would be a bar to the discharge of a bankrupt.

7. The proposal of said Arrangement and its acceptance are in good faith and have not been made or procured by any means, promises or acts forbidden by said Act.

WHEREFORE, the said American Trailer Rentals
 321 Company prays that said Arrangement be confirmed
 by the Court.

AMERICAN TRAILER RENTALS COMPANY

By **IRVIN H. PETERS'**
Executive Vice-President, Debtor

/s/ **BENJAMIN E. SWEET**
 Benjamin E. Sweet
 2550 First National Bank Building
 Denver 2, Colorado 266-3558

GILBERT C. MAXWELL
 Gilbert C. Maxwell
 2550 First National Bank Building
 Denver 2, Colorado 266-3558

/s/ **ARTHUR W. BURKE, JR.**
 Arthur W. Burke, Jr.
 1010 American National Bank
 Building
 Denver, Colorado MAin 3-4395

Attorneys for Debtor

*Duly sworn to by Irvin H. Peters
 jurat omitted in printing*

322 (Filed Mar. 8, 1963)

Minutes—March 8, 1963

33276—American Trailer Rentals Co.

Continued hearing before Special Master on Section 328 motion filed by Securities and Exchange Commission. The Commission appeared by William D. Scheid and William J. Cooney, its attorneys; and the debtor by Gilbert C. Maxwell and Arthur W. Burke, Jr., its attorneys. After hearing evidence to conclusion, the Commission and the debtor having announced no further evidence would be adduced, ORDERED, (1) that the Commission, at the earliest possible time, file with the Special Master a transcript of the evi-

dence heard on the said motion previously and on this day; (2) that upon receipt of said transcript the Special Master give notice of the filing thereof to counsel for the Commission and the debtor; and that (3) within ten days of the date of said letter the Commission and the debtor shall each file with the Special Master a brief as to their respective views, and shall serve a copy thereof each on the other and file due certificate of service with the Special Master.

Hearing on application to confirm arrangement. The debtor appeared by Irwin H. Peters, its executive vice-president, and Gilbert C. Maxwell and Arthur W. Burke, Jr., its attorneys; various creditors appeared by their respective attorneys, Martin J. Andrew and Joseph Jaudon, Jr.; and the Securities and Exchange Commission by William D. Scheid and William J. Cooney, its attorneys. Good cause having been shown, it is ORDERED that the hearing be and it is continued to April 5, 1963, at 1:30 P. M., to be then reset as the Referee shall that day determine and order.

ORDERED, pursuant to Section 38 of the Bankruptcy Act, that the debtor forthwith pay \$17.50 to Holman Mills, as an expense of administration, for attending and reporting this day's proceedings.

Upon consideration of the petition for fees filed by Gilbert C. Maxwell, Truman C. Engelhardt and Martin J. Andrew, the members of the special committee appointed by the Court to examine and report as to claims and acceptances, filed, it appearing that the petitioners performed the services in said petition described and are entitled to the compensation sought, it is, no adverse interest being represented, ORDERED, that the debtor shall forthwith pay \$250.00 to each of said members of said Committee, as an expense of administration, in full of their services as such.

/s/ Illegible
Chief Referee in Bankruptcy.

March 8, 1963.

(Hon. Benjamin C. Hilliard, Jr.)

jf

392

(File endorsement omitted)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADOIn Proceedings for an Arrangement
No. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor.***Order—May 20, 1963**

The Report and Recommendations of Benjamin C. Hilliard, Jr., Special Master, with respect to the Motion of the Securities and Exchange Commission to dismiss this proceeding under Section 328 of the Bankruptcy Act and with respect to the fees of reporters by whom transcripts were prepared and the compensation of the Special Master, coming on for hearing the 6th day of May, 1963, and the Securities and Exchange Commission appearing by William D. Scheid and William J. Cooney, its attorneys, and Debtor by Gilbert C. Maxwell and Arthur W. Burke, Jr., its attorneys, and the Court having heard the arguments of counsel,

FINDS:

1. That the Special Master's findings of fact with respect to the Motion made by the Securities and Exchange Commission, pursuant to Section 328 of Chapter XI, are proper and are accepted and adopted as findings by the Court.
2. The findings of fact and conclusions of the Special Master with reference to the reporter's fees for transcripts and the compensation to the Special Master, although proper as to amount, may not be charged to the Securities and Exchange Commission and the orders of the Special Master with reference thereto, and are erroneous and are not accepted and rejected.

It Is ORDERED,

That the Motion of the Securities and Exchange Commission pursuant to Section 328 of Chapter XI of
393 the Act relating to Bankruptcy filed herein, be and the same is hereby denied.

The report and recommendations of the Special Master insofar as they relate to payment by the Securities and Exchange Commission of costs of transcripts forwarded to the Special Master and of compensation of the Special Master are rejected and the Commission's motion to vacate the Special Master's order of March 8, 1963 directing the Securities and Exchange Commission to file a transcript is granted and that order is vacated.

Dated May 20, 1963.

ALFRED A. ARRAB
Chief Judge

Date:

Approved as to Form:

WILLIAM A. BASSETT
*Attorney for Securities and
Exchange Commission*

GILBERT C. MAXWELL /s/

ARTHUR W. BURKE, JR. /s/
Attorneys for Debtor

Entered on the Docket, May 20, 1963
By G. WALTER BOWMAN, Clerk

400 Clerk's Certificate to foregoing
transcript omitted in printing.

401 IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO.

In Bankruptcy 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor.*

Transcript of Hearing—May 3, 1963

Proceedings had before the HONORABLE ALFRED A. ARRAB,
Chief Judge, United States District Court for the District
of Colorado, beginning at 9:00 a.m., on the 3rd day of May,

1963, in Courtroom A, Main Post Office Building, Denver, Colorado.

Appearances:

WILLIAM D. SCHEID and WILLIAM J. COONEY, Attorneys at Law, Chicago, Illinois, appearing for the Securities and Exchange Commission.

GILBERT C. MAXWELL and ARTHUR W. BURKE, JR., Attorneys at Law, Denver, Colorado, appearing for the Debtor.

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Ruling of the Court

The Court: The Court is of the opinion that the Securities and Exchange Commission has failed to establish that the findings of fact and conclusions of law of the Special Master with the exception of those findings related to the cost are clearly erroneous.

Therefore, the Court will confirm and adopt the findings insofar as they pertain to the denial of the 328 motion.

As I stated at the outset of this hearing, I have studied the file in this case prior to the hearing. I listened to the arguments of counsel, and I am not convinced that the needs to be served here can best be met by a Chapter 10.

The cases that were cited and which I looked at, none of them involved a company who operated a business such as the one that we have here. It seems to me that actually there are no assets whatsoever in this corporation, except maybe some desks, some furniture, except its net work, if we may use that term, or—I think that's satisfactory—its net work of filling station operators who serve as agents to rent these trailers out to prospective users.

Now, there may be in this situation need for new management, and there certainly is some question in my mind as to whether or not the management that is presently representing it would—I mean, operating it, would continue to do so for the best interests of the investors. However, that has not been clearly established yet and if there is any indication of any criminal activity on the part of the people who are running the company, this should by the SEC be investigated and if found that there is any or has been any criminal activity should be

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reported to the proper authorities in the Justice Department.

I don't think it is the function of this Court under a Chapter 10 proceedings to—that is, the primary function—to investigate a claim of poor business management—or improper business management, or maybe even criminal action on the part of management or some officers or directors of the company. This would be—this investigation would be incidental.

I do not think the investigation can be best made by a trustee, because there are no funds with which to do this. Now, there are some funds coming in, but these funds better be used to pay the debts of the corporation, and to pay off the investors if there is sufficient funds.

It has been our experience—shall I say, my experience, in this Court, with the exception of one case under Chapter 10 that I have had, none of them work out. We spend a good bit of the money that is available on trustees and attorneys fees and we end up in worse shape than we did before.

Most of these businesses that reach this point
404 probably would be better off to be in bankruptcy as far as the creditors are concerned. In other words, they are ill. The illness is terminal and it is just a question of whether or not the life should be prolonged, I think aptly describes the situation that we find in many of these cases.

Now, I have, or, I want to express for the record some objection to the proposed plan. I do not think that the proposed plan gives the owners of the trailers a fair shake.

In other words, unless this plan that is finally determined in this case under the Chapter 11 is such a plan that the investors themselves will have control of this corporation and not the management who got it in this shape, then I say it will be an improper plan. Therefore, that would suggest that the investors should have more than one share of stock for each two dollars and management less than one share for each three dollars and a half, but at any rate, the proportion of the ratio should be such as the investors will have control of the corporation. This is the only way, in my opinion, that it can properly operate.

Now, also in connection with the plan, consideration should be given to treating all creditors alike. One creditor

should not be paid just because the officers guaranteed that payment and another creditor not paid in cash. The bank, for example. These people are knowledgeable in this business. They are sophisticated lenders, and to treat them with some special treatment as against an individual who is a creditor is not, in my opinion, equity or justice.

Now, there is still pending, as I understand it, the motion of the SEC to intervene. This is a matter to be determined by the referee, but it seems to me the SEC could very well serve a useful purpose in a Chapter 11 proceedings. They have certain expertise in the field of securities. They have certain knowledge that would be helpful. They can advise and they can also serve somewhat in a similar capacity as they do under Chapter 10. I merely pass that on for what it may be worth.

I think under the circumstances here that Chapter 11 having been first filed and the rules as I understand it that Chapter 10 should be used only if 11 is not available, which gives further weight to the conclusion that the findings of the referee are not clearly erroneous, because I think Chapter 11 is available in the state of the matter as it is presented to the Court at this time.

Now, with reference to the costs, it is my opinion that the findings of the referee in that connection, in connection with the costs, are clearly erroneous, in that costs cannot under the law be assessed against the Government unless the Congress specifically authorizes it and I don't think that has been done in connection with the proceedings of this type. Therefore, those findings with reference 405 to costs will be set aside.

In so doing, I am not saying the costs should not be paid and not just amounts. I am not finding that at all. I am just finding that they are not properly chargeable under the law to the SEC, because in effect the SEC in this instance is the Government. You cannot charge the Government with costs, I believe, unless the Congress has authorized it.

I shall ask counsel to confer and prepare a proper order of the Court in line with the comments and statements the Court has made here.

Either counsel have anything further at this time?

Mr. Maxwell: May I make one comment?

The Court: Yes.

Mr. Maxwell: I agree with some of the comments you made on the alterations on the plan and such will be presented along the line that you have suggested.

The Court: Thank you, Mr. Maxwell. You may announce recess.

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Reporter's Certificate to foregoing
transcript omitted in printing

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(Filed May 20, 1963)

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IN UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

In Proceedings for an Arrangement No. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, *Debtor*

Modification of the Proposed Plan of Arrangement—
May 20, 1963

The above named Debtor hereby proposes a modification of its proposed Plan of Arrangement with its unsecured creditors as follows:

1. That the proposed Plan of Arrangement be modified in that the unsecured creditors of the Debtor who are also officers and directors of the Debtor, receive shares of the no par value common stock of Capitol Leasing Corporation on the basis of one share for each \$5.50 of debt to them, and that they

- a. Waive dividends on such shares for five years.
- b. Limit their voting rights for five years and have one vote for each seven shares at meetings of the shareholders in the election of directors and other matters submitted to the vote of the shareholders.
- c. Waive for a period of five years any rights in the event of liquidation during said period, of Capitol Leasing Corporation,

which waivers and restrictions will be noted upon any and all certificates for shares of Capitol Leasing Corporation which may be issued to them.

2. All of said persons who are officers and directors have agreed to the foregoing and their individual agreements are attached as exhibits. In addition, other persons who hold notes of the Debtor have also agreed to the foregoing and their agreements are attached as exhibits. The officers and directors and the other note holders, the amounts of their notes and the number of shares of Capitol Leasing Corporation which they would receive upon the above basis upon confirmation are as follows:

Glenn D. Bombgardner	\$ 3,333.00	606 shares
Hammond Bros.	5,000.00	909 shares
Clair B. Mahr	2,020.00	367 shares
Jesse D. Kirklin	5,050.00	918 shares
I. H. Peters	5,833.33	1061 shares
R. J. Rutherford	8,310.00	1511 shares
Joseph L. Flores	10,580.00	1924 shares
James Monsour, M. D.	23,383.33	4252 shares
Carl Firebaugh	7,550.00	1373 shares
James H. Daly	217,170.56	39,486 shares

3. That the proposed Plan be modified in that the Denver U. S. National Bank be eliminated from consideration in the Plan and have no claim upon Capitol Leasing Corporation. The obligation of the Debtor involving \$50,810.00 has been assumed by James H. Daly and is included in the amounts due him as set forth in paragraph 2, and will be satisfied by the issuance of shares of Capitol Leasing Corporation on the basis of one share for each \$5.50 of this debt, which shares will be subject to the restrictions set forth in paragraph 1.

4. That the proposed Plan be modified in that Alexander Grant & Company be eliminated from consideration in the Plan and have no claim against Capitol Leasing Corporation. It is proposed that the note of the Debtor in the amount of \$15,557.95 held by Alexander Grant & Company be cancelled and Alexander Grant & Company receive a new note signed by the guarantors of the Debtor's note.

5. The foregoing modifications of the Proposed
542 Plan of Arrangement do not affect the position or
rights of other unsecured creditors and there need be
no further vote on the proposed Plan as to which there
has been a finding of acceptance by a majority in number
and amounts of unsecured creditors.

6. In connection with the foregoing modification of the
proposed Plan, Debtor states that Capitol Leasing Corpora-
tion has filed herein its Petition to Intervene, which
Petition proposes a further modification in that no shares
of stock of Capitol Leasing Corporation, except as neces-
sary to effect the Plan of Arrangement, shall be issued for
a period of five years unless the shareholders of Capitol
Leasing Corporation shall, in a duly called shareholders
meeting called for such purpose, authorize the issuance of
such stock.

Dated at Denver, Colorado, this 20th day of May, 1963.

AMERICAN TRAILER RENTALS COMPANY

By I. H. PETERS

I. H. Peters

Executive Vice-President

STATE OF COLORADO } ss.
CITY AND COUNTY OF DENVER }

Subscribed and sworn to before me, a Notary Public,
this 20th day of May, 1963.

My Commission expires June 14, 1964.

/s/ JAMES P. FORD
Notary Public

(SEAL)

596 Minute Entry of Argument and Submission—
September 13, 1963

(Omitted in printing)

597

(File endorsement omitted)

IN THE UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

Nos. 7392-7474—November Term, 1963.

In the Matter of

AMERICAN TRAILER RENTALS COMPANYSECURITIES AND EXCHANGE COMMISSION, *Appellant*,

v.

AMERICAN TRAILER RENTALS COMPANY, *Debtör-Appellee*.Appeal From The United States District Court
For The District of Colorado

David Ferber, Associate General Counsel, Securities and Exchange Commission, Washington, D. C., (Philip A. Loomis, Jr., General Counsel, Allan R. Roth, Attorney, Thomas B. Hart, Regional Administrator, J. Kirk Windle, Special Counsel, and William D. Scheid, Attorney, all of the Securities and Exchange Commission with him on the brief), for Appellant.

Gilbert C. Maxwell, Denver, Colorado, (Arthur W. Burke, Jr., and Benjamin E. Sweet, Denver, Colorado, with him on the brief), for Debtor-Appellee.

Opinion—Filed December 9, 1963

Before MURRAH, Chief Judge, and PHILLIPS and PICKETT,
Circuit Judges.

PICKETT, Circuit Judge.

598 This is a consolidated appeal from two orders of the United States District Court for the District of Colorado, growing out of an arrangement proceeding under Chapter XI of the Bankruptcy Act, (11 U.S.C. § 701, et seq.), in which American Trailer Rentals Company is

the debtor.¹ Securities and Exchange Commission is the appellant in both instances. The S.E.C. contends that the District Court erred in denying its motion to intervene and to dismiss the Chapter XI petition unless the proceedings were continued under Chapter X of the Bankruptcy Act. (11 U.S.C. § 501, et seq.) It is urged that the relief afforded by Chapter XI is inadequate because the circumstances disclosed by the record indicate the necessity of an independent investigation of the proposed new management and the methods used in soliciting approval of the plan, which can be accomplished only in a Chapter X proceeding.

599 The debtor is a Colorado corporation organized in 1958 to engage in the business of renting automobile trailers to the general public for local and cross-country trips. Originally, the trailer rental system had been operated by a complex of inter-related corporations, of which the debtor was one. In 1961, the remaining corporations of the complex were merged into the debtor. Under the rental system as operated by debtor, trailers were sold to individuals and leased back to the debtor. These trailers are the ordinary, utility type, which may be attached to the rear of an automobile by means of a detachable bumper hitch furnished as part of the trailer equipment. The trailers were placed at gasoline service stations in several states, with individual station operators acting as rental agents for the debtor.²

Under the sale-and-lease-back contracts with the individual trailer owners, the debtor had agreed to a fixed return per year, based on the cost of the trailer. Three payment plans were used, (1) a guaranteed payment of 2% per

¹ No. 7392 is an appeal from a denial of the Commission's application under Section 328 of the Bankruptcy Act, (11 U.S.C. § 728), to dismiss the debtor's petition under Chapter XI, on the ground that it should properly be a Chapter X proceeding.

No. 7474 is an appeal from an order denying the Commission's motion to intervene in the Chapter XI proceedings to show a violation of Section 17 (fraud provisions) of the Securities Act of 1933, and confirming the arrangement as modified.

² When the petition herein was filed, these agents, scattered throughout the country, numbered about 500.

month for 10 years, (2) a guaranteed payment of 600 3% per month for 5 years, and (3) a payment of 35% of the rental income less repairs. A majority of the agreements were for 2% per month for 10 years. The debtor, in its proposed arrangement, stated that these fixed payments, since unrelated to the actual earnings of the trailers, were the major cause of its financial difficulties.

When the petition was filed on December 20, 1962, the debtor stated its assets to be \$685,608.82, and its liabilities \$1,367,890.66.³ Its trailer network consisted of approximately 3,000 trailers, owned by about 1,200 individuals, and located throughout the country at the rental stations. Debtor's peak earnings had been \$60,000 per month, but diminished to about \$14,000 per month when this 601 proceeding was instituted, and was down to \$4,000 per month when the Commission's petition was filed. Considering the payments made under the leasing agreements as a return of capital, the trailer owners' remaining investment in the 3,000 trailers totaled \$1,532,902.43.

The arrangement proposed, as modified, provides that the trailer owners would transfer title to their trailers in exchange for one share of stock in the newly created

³ Assets:

\$ 500,000.00	rental network (intangible asset)
173,196.07	accounts receivable
10,712.75	furniture and equipment
1,700.00	vehicles and service equipment

\$ 685,608.82

Liabilities:

\$ 5,611.58	secured debt (chattel mtgs. on furniture, vehicles and service equipment)
727,585.97	executory contracts
230,783.29	accounts payable
392,533.15	notes payable
6,691.97	wages and commissions
4,684.70	taxes

\$ 1,367,890.66

(From Referee's Statement)

Capitol Leasing Corporation,⁴ for each two dollars of their remaining investment in exchange for the title to the trailers, and forego their claims for past and future payments growing out of their leasing agreements. Persons who had paid in \$200,677 for trailers which were never manufactured are to receive one share for each \$2.00 paid.⁵ The trailer rental system is to be assigned to Capitol Leasing in exchange for 107,100 shares. Unsecured creditors are to receive one share for each \$3.50 of debt, except those unsecured creditors who are also officers and directors of the debtor, who are to be given one share for each \$5.50 of debt. A \$40,000 bank debt is to be assumed by the president of the debtor and he will receive one share for each \$5.50 of the assumed obligation. The amount due the accountants is to be paid by individual officers and directors of the debtor as guarantors of debtor's note. The court expressed some objection to the initial arrangement, indicating that it did not appear to give the trailer owners a "fair shake." It was indicated that an acceptable plan should be one which resulted in the investors' control of the corporation, and noted that investors should perhaps get more than one share for each \$2.00 of investment, while management should get less than one share for each \$3.50 as was originally proposed. Following those comments, debtor submitted the amendments to the arrangement.

The Commission, in its motion under Section 328 of the Bankruptcy Act, 11 U.S.C. § 728, to dismiss the Chapter

⁴ Capitol Leasing Corporation was formed on March 27, 1962, for the purpose of salvaging debtor's business. In May of that year, it commenced the public offering of its shares under the Regulation "A" Exemption, Securities Act of 1933, in exchange for cash or trailers. Only trailers were exchanged. On October 9, 1962, the S.E.C. stop-ordered the Regulation "A" offering on the grounds that the notification and offering circular were false and misleading. By that time, Capitol Leasing had acquired 299 trailers in exchange for 88,332 shares of its no-par stock, on the basis of one share for each \$2.00 of investment. The only outstanding shares of Capitol's authorized 3,200,000 shares are those issued in exchange for the trailers prior to the stop-order.

⁵ This amount was paid to DeMar, Inc., a Nebraska corporation, which in 1960 was granted the exclusive right to manufacture trailers for the system, but has since been adjudicated a bankrupt.

XI proceedings, alleges that this is properly a Chapter X proceeding for three reasons:⁶ first, that the debtor needs more than just an arrangement with its unsecured creditors; second, that the public investors need a disinterested trustee to protect and enforce their rights; and third, that Chapter X is required so that public investors will receive fair and equitable treatment. Since a petition for reorganization under Chapter X cannot be filed if "adequate relief would be obtainable by a debtor's petition under . . . Chapter XI" (§ 146(2), Bankruptcy Act; 11 U.S.C. § 546(2)), the ultimate question is whether "adequate relief" is obtainable under the debtor's proposed arrangement.⁷ Chapter XI does not require that the arrangement be "fair and equitable" as does Chapter X; (§ 221(2), Bankruptcy Act, 11 U.S.C. § 621(2)), but only that it be feasible and in the best interest of the creditors. (§ 366(2), Bankruptcy Act, 11 U.S.C. § 766(2)). The essential consideration in the choice between Chapter X and XI is "the needs to be served." General Stores Corp. v. Shlensky, 350 U.S. 462, 466. Although Chapter XI is limited to arrangements dealing with unsecured debts,

⁶ Title 11, U.S.C. § 728, provides:

"The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under Chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter."

⁷ The judge may, upon application and notice, dismiss a Chapter XI petition if he finds that the proceedings should have been brought under Chapter X. (§ 328, Bankruptcy Act, 11 U.S.C. § 728). This determination rests in his sound judicial discretion. General Stores Corp. v. Shlensky, 350 U.S. 462; S.E.C. v. Wilcox-Gay Corp., 6 Cir., 231 F.2d 859; In re Transvision, Inc., 2 Cir., 217 F.2d 243, cert. denied 348 U.S. 952.

(§ 306(1) Bankruptcy Act, 11 U.S.C. § 706(1)), the mere existence of public investors does not preclude the use of Chapter XI. General Stores Corp. v. Shlensky, *supra*; Grayson-Robinson Stores, Inc. v. S.E.C., 2 Cir., 320 F. 2d 940. However, the more complex the debt structure and stock distribution, the greater the likelihood that the more complex procedures and safeguards of Chapter X are required. In re Transvision, 2 Cir., 217 F. 2d 243, cert. denied 348 U.S. 952; Grayson-Robinson Stores, Inc. v. S.E.C., *supra*.⁸

The Securities Exchange Commission argues that the arrangement as proposed by debtor is not really an arrangement at all, because if the plan is effected, the creditors of the debtor will be transformed into shareholders of the new corporation. The arrangement indicates that there is an aggregate remaining capital investment in the trailers of \$1,532,902.43, which includes unpaid leasing fees in the amount of \$710,597.53. There-

⁸ Chapter X involves more complex procedures and safeguards than does Chapter XI. Chapter X requires the appointment of an independent trustee, the investigation of the activities and affairs of the debtor, the plan or reorganization as formulated by the trustee, the S.E.C. participating in an advisory capacity, and the creditors' committees subject to judicial control and scrutiny. See, generally, Collier on Bankruptcy, 14th Ed. Vol. 6, §§ 0.08[3], 0.09.

Although not expressly limited to the use of large corporations, Chapter X was, in effect, designed for the larger corporation with shares widely held by the public and with complicated debt structures. S.E.C. v. U.S. Realty Co., 310 U.S. 434. However, the choice between Chapter X and Chapter XI "is not determined solely by the size and capital structure of the company but, rather, by the nature of the interested parties, the necessity for independent investigation and control, the degree to which the debtor's activities must be readjusted." Collier on Bankruptcy, 14th Ed. Vol. 6, 1962 Supp. p. 7.

Factors appropriate to a Chapter XI arrangement include (1) simple corporate structure, (2) more than half the common stock held by management, (3) no interference with shareholder's rights, (4) acceptance of plan by unsecured creditors, (5) provision for priority creditors, (6) inability of corporation to bear expense of Chapter X proceeding. In re Lea Fabrics, 3 Cir., 272 F.2d 769, vacated as moot sub. nom. S.E.C. v. Lea Fabrics, Inc., 363 U.S. 417. Collier on Bankruptcy, 14th Ed. Vol. 6, 1962 Supp. p. 7.

fore, debtor states that trailer owners are to be compensated for their claims at the rate of one share for each \$2.00 since the plan states that 766,451 shares of Capitol Leasing will be required to acquire title to all the trailers.⁹ As the S.E.C. points out, there is no provision in the arrangement for trailer owners who do not choose to exchange their trailers for stock. In such cases the owners would retain title and the right of possession to their trailers.

The Commission also infers that debtor's remarks concerning a need for additional financing in order to salvage the business, and the implication that debtor's management may have engaged in some mishandling of corporate

funds, supports the position that an independent

trustee such as Chapter X provides, is necessary to

assure fair and equitable treatment of public investors. The S.E.C. states that the most serious aspect of unfairness relates to the compensation of debtor's shareholders, as compared to the trailer owners. The S.E.C. argues that in the absence of a fresh contribution of capital, the stock-holders are entitled to receive nothing until the creditors (the trailer owners) are compensated in full, and that to do otherwise, as the plan contemplates, would be a violation of the absolute priority rule as laid down in *Case v. Los Angeles Lumber Products Co.*, 308 U.S. 106,¹⁰ reh. denied 308 U.S. 637. But See

⁹ Debtor assumes that the leasing fees previously paid trailer owners constituted a return of capital; if so, trailer owners would appear to receive compensation for their claims.

¹⁰ The 1952 Amendment of § 366(2), Bankruptcy Act, 11 U.S.C. § 766(2), (66 Stat. 433, P.L. 456, 82d Cong. 2d Sess. § 35) eliminated from Chapter XI proceedings the "fair and equitable" provision, since in *S.E.C. v. U.S. Realty Co.*, 310 U.S. 434, it was held that they were "words of art" having a well-understood meaning requiring an application of the principles of priority. The Court stated (310 U.S. 434, 452) that:

"The phrase signifies that the plan or arrangement must conform to the rule of *Northern Pacific Ry. Co. v. Boyd*, 228 U.S. 482, which established the principle which we recently applied in the *Los Angeles* case, [*Case v. Los Angeles Lumber Products Co.*, 308 U.S. 106, reh. denied 308 U.S. 637] that in any plan of corporate reorganization unsecured creditors are entitled to priority over stockholders to the full extent of their debts and that any scaling down of the claims of creditors without some fair compensating

608 tion 366 states in part, that "Confirmation of an
arrangement shall not be refused solely because the
interest of a debtor, or if the debtor is a corporation, the
609 interests of its stockholders or members will be
preserved under the arrangement." In the legisla-
tive history of the 1952 amendments relating to
Section 366, it is stated:

"The proposed amendment is designed to remove the
fair and equitable provision, and by the paragraph
added to each of the amended sections it is made clear
that the rule of the Boyd and Los Angeles cases shall
not be operative under those three chapters. [Chapters
XI, XII, XIII]." U.S. Code, Cong. and Adm. News,
82d Cong. 2d Sess. 1952, p. 1982.

advantage to them which is prior to the rights of stockholders is
inadmissible."

However, Chapter XI is derived from the composition procedure
of the former § 12 of the Bankruptcy Act, in which the fair and
equitable rule did not apply. The essence of Chapter XI is to
permit the scaling down of debts, while allowing the debtor to
keep his business and property. While this may be in the best
interests of the creditors, it is contrary to the principles of priority
expressed in the Boyd and Los Angeles Lumber cases. But the
rule of those cases "cannot realistically be applied in a Chapter
XI proceeding. Were it so applied, no individual debtor and,
under Chapter XI, no corporate debtor where the stock ownership
is substantially identical with management could effectuate an
arrangement except by payment of the claims of all creditors in
full." U.S. Code Cong. & Adm. News, 82d Cong. 2d Sess. Vol. 2,
1952, pp. 1981-2; Hanna & MacLachlan, *The Bankruptcy Act*
Annotated, Foundation Press, 1957, pp. 246-7.

But see, S.E.C. v. Liberty Baking Corp., 2 Cir., 240 F.2d 511,
cert. denied 353 U.S. 930, which indicates that the "fair and
equitable" rule may be applied in determining whether Chapter
X or Chapter XI should be used. If the arrangement proposed
to be accomplished under Chapter XI contains features which bring
it within Chapter X, then an application of the "fair and equi-
table" rule is relevant. However, if the plan is properly within
Chapter XI, it does not have to measure up to that standard.
Collier on Bankruptcy, 14 Ed. Vol. 9, § 9.18 [2.1]. Collier states
that "Since the legislative elimination of the 'fair and equitable'
test, use and reliance on these words, in view of their past inter-
pretation, should not be continued. While several decisions have
continued to refer to the 'fair and equitable' test, other and sound
reasons for favoring Chapter X over Chapter XI were present
in those cases." *Id.* at p. 306.

S.E.C.'s position begs the question since it assumes that the arrangement has features which require the procedures of Chapter X. See S.E.C. v. Liberty Baking Corp., 2 Cir., 240 F. 2d 511, cert. denied 353 U.S. 930. However, since the granting of the motion rests in the discretion of the court, while we think this is a border-line case, it does not appear that the S.E.C. has shown that adequate relief is not obtainable in Chapter XI proceedings or that there has been an abuse of that discretion warranting reversal.

The second order appealed from relates to the confirmation of the arrangement as modified, and the denial of S.E.C.'s request to intervene to show violations of Section 17 (fraud provisions) of the Securities Act of 1933, (15 U.S.C. § 77q). While Securities issued under Chapter XI proceedings are exempt from Section 5 (registration) under the Securities Act of 1933, (15 U.S.C. § 77e), they are 610 not exempt from Section 17.¹¹

The S.E.C. alleges that at the time debtor was sending letters to the trailer owners urging them to exchange their trailers for shares of Capitol Leasing stock, the president of Capitol and the officers and directors of the debtor were withdrawing their trailers from debtor and were leasing them to another concern engaged in a similar business, and were also urging their relatives to do the same. This was not disclosed to the trailer owners, nor were trailer owners furnished information of Capitol's financial condition or its management. Trailer owners were not told of pending proceedings involving other stock fraud charges against Capitol.

The S.E.C. has on two prior occasions stopped the sale of securities by debtor and Capitol. The first was with regard to debtor in 1961 when the S.E.C. informed debtor that its trailer rental plans were investment contracts and, therefore, securities requiring registration. A registration statement was filed, but never became effective, and 611 the issue was stop-ordered on the ground that the statement contained false and misleading statements and omitted certain material facts. The second involved

¹¹ Section 3(a)(10), Securities Act of 1933, 15 U.S.C. § 77e(a)(10); Section 17(e), Securities Act of 1933, 15 U.S.C. § 77q(e); Section 393, Bankruptcy Act, 11 U.S.C. 793.

the shares issued under the Regulation "A" exemption by Capitol Leasing Company in exchange for trailers. (See, footnote 4, *supra*).

The S.E.C. also notes a number of other omissions of facts which it considers material if the investors are to be able to make an informed judgment on the arrangement. S.E.C. contends that the circumstances surrounding the offering of Capitol Leasing stock under the arrangement is even more unfavorable and with less disclosure than the offering of Capitol under the Regulation "A" exemption which was stop-ordered.

Under Section 17(a), Securities Act of 1933, 15 U.S.C. § 77q(a), the failure to state the whole truth with regard to a security is equally as unlawful as statements of half-truths or deliberate falsehoods. *Hughes v. S.E.C.*, C.A. D.C., 174 F. 2d 969. It is the impression created by the statements which determines whether they are misleading. *Kalwajtys v. F.T.C.*, 7 Cir., 237 F. 2d 654, cert. denied 352 U.S. 1025; *S.E.C. v. Macon*, D.C. Colo., 28 F. 612 Supp. 127. Cf. *Berko v. S.E.C.*, 2 Cir., 316 F. 2d 137.

Section 17(a) is not limited to the common-law definition of fraud. *Hughes v. S.E.C.*; *supra*; *Norris & Hirshberg v. S.E.C.*, C.A. D.C., 177 F. 2d 228, cert. denied 333 U.S. 867; *Loss, Securities Regulation*, 1 Vol. Ed. p. 1435. From the authorities, it appears that if the stock involved here were not part of an arrangement, the disclosures made with regard to it would be clearly inadequate. No authority has been found which would indicate that recipients of stock issued in connection with an arrangement are not entitled to as much information as are those persons acquiring stock under ordinary conditions.

The S.E.C. points out in its brief that the simplest procedure would be for debtor to voluntarily provide the needed information,¹² and, failing in that, the referee should

¹² In its brief, the S.E.C. states:

"It has been the Commission's position throughout that the simplest and most efficient resolution of the issue it has raised would be for the debtor and Capitol to send to trailer owners a statement or letter containing the material facts to which they are entitled. Had this been done, there would have been no need for this appeal or the expensive and time-consuming antecedent proceedings. Trailer owners could have been resolicited to accept the arrangement on the basis of adequate and accurate information."

have ordered that disclosure be made. We think
 613 this is a matter which the District Court can now handle. If it appears that, for the protection of those being solicited to accept the plan, additional information is necessary, the Court should so order. The Court has directed that the stock ratio for Capitol Leasing be such that the creditors will have control of the new corporation. In proceedings such as this, the District Court retains jurisdiction until the plan is carried out. §§ 368, 369, Bankruptcy Act, 11 U.S.C. §§ 768, 769. It may be that even without the additional information, the arrangement would still be in the "best interests of the creditors" (§ 366, 11 U.S.C. § 766), since that involves a comparison between what they will receive under the arrangement and what they would receive on liquidation. *In re Village Men's Shops, Inc.*, D.C. Ind., 186 F. Supp. 125. The debtor has little or no tangible assets, and if it were liquidated it is not unlikely that the trailer owners, or at least many of them, would have difficulty realizing anything for their trailers.¹³

614 For an arrangement to be "feasible," the creditors must be assured of receiving what is promised them under the arrangement, but it does not require an assurance of future business success. *In re Slumberland Bedding Co.*, D.C. Md., 115 F. Supp. 39.

AFFIRMED.

615 UNITED STATES COURT OF APPEALS
 FOR THE TENTH CIRCUIT

Before Honorable Alfred P. Murrah, Chief Judge, and Honorable Orie L. Phillips and Honorable John C. Pickett, Circuit Judges.

¹³ In the debtor's proposed arrangement, it was stated:

"Unless the plan is adopted, proponents suggest that creditors will receive little, if anything, in settlement of debtor's obligation to them, and that trailer owners may find themselves unable to realize any value for their trailers or any income from their operation."

Judgment—December 9, 1963

These causes came on to be heard on the transcript of the record from the United States District Court for the District of Colorado and were argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the judgment of the said district court in these causes be and the same is hereby affirmed.

By order of January 21, 1964, the mandate of the United States Court of Appeals was stayed for a period of thirty days under the provision of paragraph 3 of Rule 28 of said court.

616 (Clerks' Certificates to foregoing transcript omitted in printing.)

618 SUPREME COURT OF THE UNITED STATES

No. 828—October Term, 1963

SECURITIES AND EXCHANGE COMMISSION, *Petitioner*,

v.

AMERICAN TRAILER RENTALS COMPANY

Order Allowing Certiorari—March 23, 1964

The petition herein for a writ of certiorari to the United States Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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In the Supreme Court of the United States

OCTOBER TERM, 1963

No. —

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

AMERICAN TRAILER RENTALS COMPANY

**PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE TENTH CIRCUIT**

The Solicitor General, on behalf of the Securities and Exchange Commission, petitions for a writ of certiorari to review that portion of the judgment of the United States Court of Appeals for the Tenth Circuit entered on December 9, 1963, that affirmed the order of the district court denying the Commission's motion to dismiss this proceeding under Chapter XI of the Bankruptcy Act.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, pp. 1a-13a) is not yet reported. The oral ruling of the district court (App. B, *infra*; pp. 14a-17a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on December 9, 1963 (App. C, *infra*, pp. 18a-19a).

The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a corporate rehabilitation under the Bankruptcy Act affecting the rights of widespread public investor-creditors, including a scaling down of their claims for the benefit of stockholders, may be conducted under Chapter XI of the Bankruptcy Act or whether transfer to Chapter X is required.

STATUTE INVOLVED

Chapters X and XI of the Bankruptcy Act (11 U.S.C. 501, *et seq.*, and 701, *et seq.*) are involved in this proceeding substantially in their entirety. The following sections are particularly pertinent:

Section 216(1) (11 U.S.C. 616(1)):

A plan of reorganization under this chapter—

(1) shall include in respect to creditors generally or some class of them, secured or unsecured, and may include in respect to stockholders generally or some class of them, provisions altering or modifying their rights, either through the issuance of new securities of any character or otherwise;

Section 306(1) (11 U.S.C. 706(1)):

For the purposes of this chapter, unless inconsistent with the context—

(1) “arrangement” shall mean any plan of a debtor for the settlement, satisfaction, or extension of the time of payment of his unsecured debts, upon any terms;

Section 328 of the Bankruptcy Act (11 U.S.C. 728) provides:

The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter.

STATEMENT

The issue in this case is whether these proceedings for the financial rehabilitation of the respondent corporation may be conducted as an arrangement under Chapter XI of the Bankruptcy Act rather than as a corporate reorganization under Chapter X of that Act. It arises from the denial of an application of the Securities and Exchange Commission pursuant to Section 328 of the Bankruptcy Act (11 U.S.C. 728), which provides that the judge, upon application of the Securities and Exchange Commission or any party in interest, if he finds that proceedings for an

arrangement under Chapter XI "should have been brought under chapter 10," may dismiss the Chapter XI proceedings unless, within the time fixed by him, the debtor or its creditors attends the petition "to comply with the requirement of chapter 10."

1. THE RESPONDENT'S ORGANIZATION AND OPERATIONS

The respondent ("the debtor") was organized in 1958 to engage in the automobile trailer rental business (R. 3, 24). The trailers are of the general utility type which are attached to the rear bumper of an automobile (R. 3, 26). They are kept at gasoline service stations, the operators of which act as rental agents for the debtor (*ibid.*). When the petition for an arrangement was filed, the debtor had about 500 such service station agents (R. 3). The trailer rental system was originally operated by a complex of separate corporations, including the debtor, but in 1961 all the companies were merged into the debtor (R. 36, 102, 140-41, 190).

The individual trailers were sold to public investors under an agreement by which the owner leased the trailer back to the debtor for leasing to the public, and the debtor agreed to pay the owner a fixed rental (R. 3). Most of the trailers were sold under agreements to pay the owners a fixed percentage of the purchase price of the trailer—either 2 percent per month for 10 years (which was the basis upon which a majority of the trailers were sold) or 3 percent per month for 5 years (R. 3, 26). In addition, a comparatively small number of trailers were sold under an agreement by which the owner

received his respective share of 35 percent of the total rental income (less repair costs) produced by the trailers of those selecting this method of payment (R. 26). The debtor sold 5,866 trailers to hundreds of investors throughout the Western States for an aggregate price of \$3,590,168 (R. 24). The debtor also had received \$200,677 from public investors for trailers which, as the result of the insolvency of an affiliated corporation, were never manufactured and, therefore, never delivered to the purchasers or introduced into the rental system (R. 2, 37, 76-77, 82).

In 1961, after the Commission had informed the debtor that the sales of the trailers under these arrangements constituted an investment contract and therefore a security required to be registered under the Securities Act of 1933, the debtor discontinued sales of the trailers. In March 1962, persons affiliated with the debtor organized Capitol Leasing Corporation ("Capitol") (R. 132-134, 231), which offered to exchange its stock for trailers or to sell the stock at \$2.00 a share (R. 338). After Capitol had acquired 299 of the trailers in exchange for stock, the Commission temporarily suspended the exemption from registration upon which Capitol had relied in making this offer, on the ground that there was reasonable cause to believe that the material used in making the offer contained false and misleading statements (R. 335-337).¹

¹ It had relied upon the conditional exemption from registration provided for small issues under Regulation A (17 C.F.R. 230.251 *et seq.*) adopted by the Commission under Section 3(a) of the Securities Act of 1933 (15 U.S.C. 77c(a)).

2. THE CHAPTER XI PROCEEDINGS

On December 20, 1962, the debtor filed in the United States District Court for the District of Colorado a petition for and a proposed plan of arrangement under Chapter XI of the Bankruptcy Act (R. 1-7). It stated that its total assets were \$685,608, of which \$500,000 represented the value of its trailer rental system, i.e., its arrangements with the service station operator agents (R. 318). Its stated liabilities were \$1,367,890, of which \$710,597 was owed to trailer owners under their leasing agreements and \$200,677 was owed to investors who had paid for but had not received trailers (R. 4). In addition, trade and general creditors had claims of \$78,498, officers and directors had claims for loans to the corporation of \$285,277, an accounting firm was owed \$15,500, and there was an outstanding bank loan of \$40,000 (R. 4).

Under the proposed arrangement, trailer owners are to sell their trailers to Capitol in exchange for Capitol's stock (R. 4-5). They are to receive one share for every \$2.00 of "remaining capital investment in the trailers," which is to be determined by deducting from the original purchase price of the trailer the amount which the owners had received as rental payments (R. 3-4, 5). No additional compensation to the owners is provided for the \$710,000 of unpaid rentals (R. 5, 6). Owners who elect not to exchange their trailers for Capitol's stock receive nothing under the plan (R. 4-5, 6). Investors who paid for but had not received trailers will receive one share of stock for each \$2.00 of the purchase price (R. 6).

Trade and general creditors are to receive one share of stock for each \$3.50 of their claims (R. 6).

The plan of arrangement provides that the debtor will transfer its system to Capitol in exchange for 107,000 shares, which the debtor will then distribute to its stockholders (R. 7). More than 60 percent of the debtor's stock is held by ten men; nine of them are officers and directors and the tenth is one of the original promoters of the venture (R. 32, 31). The plan further provides that officers and directors will receive one share of Capitol stock for each \$5.50 of their claims for loans to the debtor, and that for five years such stock will have limited voting, dividend and liquidation rights (R. 540-542).³

3. THE MOTION TO TRANSFER THE PROCEEDINGS TO CHAPTER X

On February 20, 1963, the Securities and Exchange Commission filed a motion under Section 328 of the Bankruptcy Act to dismiss the Chapter XI proceed-

³The plan originally provided that officers and directors would receive one share for each \$3.50 of their claims (R. 6). When the district judge denied the Commission's motion to dismiss the proceedings (see below), he further stated (App. B, *infra*, p. 16a) that "I do not think that the proposed plan gives the owners of the trailers a fair shake. In other words, unless this plan that is finally determined in this case under the Chapter 11 is such a plan that the investors themselves will have control of this corporation and not the management who got it in this shape, then I say it will be an improper plan." The debtor then modified the plan to reduce the participation of its officers and directors from one share for each \$3.50 of their claims to one share for each \$5.50, and also to change the method for discharge of the debtor's bank loan and its indebtedness for accounting services (R. 540-542).

ings on the ground that the "proceedings should have been originally brought under Chapter X of the Bankruptcy Act because the Debtor's circumstances and capital structure are such that the relief afforded by Chapter XI is inadequate to satisfy the needs to be served" (R. 8). Any attempt to rehabilitate the debtor under Chapter XI, the Commission contended, would be inadequate and inconsistent with the policy of the Bankruptcy Act (R. 47-51). The Commission pointed out that whereas an arrangement under Chapter XI may affect only unsecured debts, the very plan proposed by the debtor demonstrated that more than such an arrangement was needed, since under the proposed arrangement stockholders of the debtor would participate in the successor enterprise while public investor creditors would be called upon to accept less than the full amount of their claims (R. 52). The Commission also urged that the circumstances required investigation of past management and an accounting, which could be provided only under Chapter X (R. 51).

The motion was referred to a referee in bankruptcy as special master for hearing and report (R. 55). After hearing, he recommended that the motion be denied, on the ground that the Commission had not demonstrated that adequate relief was unobtainable under Chapter XI (R. 238-40, 242), and that final "determination of the Section 328 motion ought to be postponed to the confirmation hearing [on the arrangement]" (R. 239). The district court confirmed and adopted the special master's findings, and denied the Commission's motion (R. 392-93). The

court stated that it was "not convinced that the needs to be served here can best be met by a Chapter X"; and that although "there may be in this situation need for new management, and there certainly is some question in my mind as to whether or not the management that is presently [operating] it * * * would continue to do so for the best interests of the investors * * * that has not been clearly established yet * * *" (App. B, *infra*, p. 15a).

The court of appeals affirmed. It stated (App. A, *infra*, p. 10a) that "since the granting of the motion rests in the discretion of the court, while we think this is a border-line case, it does not appear that the S.E.C. has shown that adequate relief is not obtainable in Chapter XI proceedings or that there has been an abuse of that discretion warranting reversal."³

³ The Commission had also filed a petition to intervene in the Chapter XI proceedings to show that, in violation of the antifraud provisions of the Securities Act of 1933, the information which the debtor used in procuring acceptances of the plan of arrangement was false and misleading (R. 323-352). As the court of appeals explained (App. A, *infra*, p. 11a), the Commission alleged, among other things, that "at the time debtor was sending letters to the trailer owners urging them to exchange their trailers for shares of Capitol Leasing stock, the president of Capitol and the officers and ~~directors~~ of the debtor were withdrawing their trailers from debtor and were leasing them to another concern engaged in a similar business, and were also urging their relatives to do the same. This was not disclosed to the trailer owners, nor were trailer owners furnished information of Capitol's financial condition or its management. Trailer owners were not told of pending proceedings involving other stock fraud charges against Capitol."

After hearing, a referee in bankruptcy denied the petition to intervene (R. 412-417), the district judge granted the peti-

REASONS FOR GRANTING THE WRIT

This case presents the important question whether widely scattered public investor-creditors of a financially distressed corporation can be deprived of the safeguards afforded by a thoroughgoing reorganization under Chapter X of the Bankruptcy Act—including an independent trustee, a full investigation and an impartially formulated plan of reorganization—through recourse to an arrangement under Chapter XI, where none of those protections are provided and where the rehabilitation is controlled by the management of the debtor.

We submit that Chapter XI is available only for adjustments involving trade or commercial creditors, and cannot be used to affect adversely the interests of public investor-creditors. This is so for two reasons: *First*, it would be inappropriate to adjust the rights of public creditors without giving them the benefit of the protective procedures which Congress provided in Chapter X for investors generally. *Second*, since

tion to intervene but denied the relief sought (R. 596-597), and the court of appeals affirmed (App. A, *infra*, pp. 10a-13a). The Commission's appeal on the intervention issue was consolidated with the appeal from the denial of dismissal (*id.*, p. 1a). The court of appeals agreed that "if the stock involved here were not part of an arrangement, the disclosures made with regard to it would be clearly inadequate" and that there was no basis for holding that the creditor-investors here "are not entitled to as much information as are those persons acquiring stock under ordinary conditions" (App. A, *infra*, p. 12a). It concluded, however, that appropriate action could be taken by the district court. We are not seeking review of the court of appeals' ruling on this aspect of the case.

an arrangement under Chapter XI need not satisfy the "fair and equitable" standard which a plan of reorganization under Chapter X must meet, use of Chapter XI would permit a reduction in the rights of investor-creditors in order to give the junior security holders who control the management an interest in the reorganized company. In refusing to transfer this case, the courts below failed to follow these standards, reached a result which conflicts in principle with a leading decision of the Second Circuit (*Liberty Baking, infra*, pp. 16, 18), and departed from the teaching of *Securities and Exchange Commission v. United States Realty and Improvement Company*, 310 U.S. 434, and *General Stores Corp. v. Shlensky*, 350 U.S. 462. For in the latter cases this Court made it clear that "where c. X affords a more adequate remedy than c. XI" (*General Stores*, 350 U.S. at 467), "it was plainly the duty of the district court in the exercise of a sound discretion to have dismissed the [Chapter XI] petition, remitting respondent if it was so advised to the initiation of a proceeding under Chapter X, in which it may secure a reorganization which, after study and investigation appropriate to its corporate business structure and ownership, is found to be fair, equitable and feasible, and in the best interest of creditors" (*Realty*, 310 U.S. at 456-457).

1. (a) In the *Realty* case this Court discussed the evils which led Congress to adopt the reorganization provisions of the Bankruptcy Act, and described in detail the greater protections which Chapter X provides for investors. It pointed out (310 U.S., at 418) that among the conditions which were responsible for

the enactment of Section 77B of the Bankruptcy Act, the predecessor to Chapter X, were—

* * * the inadequate protection of widely scattered security holders, the frequent adoption of plans which favored management at the expense of other interests, and which afforded the corporation only temporary respite from financial collapse * * *

In order to protect public investors from overreaching by management in the formulation and implementation of reorganization plans, Congress provided in Chapter X a comprehensive system of safeguards to be administered under the supervision of the district court. Chapter X requires (except where liabilities are less than \$250,000) the "appointment of a disinterested trustee" who is to conduct "a thorough examination and study * * * of the debtor's financial problems and management" and "to send the report to all security holders." It is the trustee, and not the management, who formulates a plan of reorganization. After the judge approves the plan, it is submitted with detailed information to creditors and stockholders for approval and, if they approve it, then is submitted to the district judge for confirmation. See 310 U.S. at 449-450.

"No comparable safeguards [to those provided in Chapter X] are found in Chapter XI" (*id.* at 450). It "provides a summary procedure by which a debtor may secure judicial confirmation of an 'arrangement' of his unsecured debts" (*id.* at 446). "Every phase of the procedure bearing on the administration of the estate and the development of the arrangement is

under the control of the debtor. The process of formulating an arrangement and the solicitation of consent of creditors, sacrifices to speed and economy every safeguard, in the interest of thoroughness and disinterestedness, provided in Chapter X. * * * The debtor proposes the arrangement * * * and the only opportunity afforded the creditors in respect to the proposed plan is to accept or reject it as submitted by the debtor. * * * There are no provisions for an independent study of the debtor's affairs by court or trustee, or for advice by them to creditors with respect to their rights or interests in advance of their consent to the arrangement. * * * The court in passing upon the arrangement, is * * * faced with the fact that a majority of the creditors have already accepted the plan." *Id.*, at 450-451. In short, any successful "arrangement" of the rights of creditors "if accomplished at all, must be without the aids to the protection of creditors and the public interest which are provided by Chapter X * * *". (*id.* at 453).

The Court concluded (p. 455) that "the adequacy of the relief under Chapter XI must be appraised in comparison with that to be had under Chapter X, and in the light of its effect on all the public and private interests concerned including those of the debtor."

* The Court reaffirmed these principles in the *General Stores* case, where it held that the lower courts there had properly transferred a Chapter XI proceeding to Chapter X. It explained that in *Realty* it had "emphasized the need to determine on the facts of the case whether the formulation of a plan under the control of the debtor, as provided by c. XI, or the formulation of a plan under the auspices of disinterested trustees, as assured by c. X and the other protective provisions of

(b) In the present case adequate protection of the public investor-creditors plainly requires resort to Chapter X. The typical investor-creditor in American has (1) a trailer located at some gasoline service station which may be hundreds of miles from his residence, (2) the "right" to receive a fixed rental for the trailer, and (3) a substantial claim against the debtor for past rentals or, in the case of investors who had paid for but not received their trailers, for the purchase price. The proposed arrangement requires the owners to accept shares of stock in a corporation organized in 1962 by persons affiliated with the debtor, on the basis of one share of stock for every \$2.00 of their "remaining capital investment." This is to be calculated, however, on the basis that all rentals which the owners had received were actually a return of capital rather than, as they had been told when they made their investment, income. They receive nothing for unpaid rentals, which total more than \$700,000. While the investors are given the right to accept or reject the plan, realistically they are under tremendous pressure to accept, no matter how unfair it may seem. For if they reject, their entire claim against the debtor for back rentals is wiped out and they are left with only a trailer, probably far away, on which they are unlikely to realize more than a small fraction of their investment.

that chapter, would better serve the public and private interests concerned including those of the debtor.' * * * [T]he controlling consideration in a choice between c. X and c. XI * * * is * * * the needs to be served" (350 U.S. at 465-466).

Although the investor-creditors are thus giving up under pressure a sizable portion of their claims against the debtor, members of the debtor's management, who are responsible for its present financial difficulties, will retain a significant interest in the successor company on the basis of their stock interest. Moreover, the old management is permitted to continue to operate the company, even though the district court recognized that "there may be in this situation need for new management" and stated that "there certainly is some question in my mind as to whether or not the management that is presently * * * operating it, would continue to do so for the best interests of the investors" (App. B, *infra*, p. 15a).

In short, this is a classic example of the kind of situation against which the safeguards of Chapter X were designed to protect public investors. There is no one to protect the interest of the investor-creditors, no one to develop and present to them the facts which they should have in order to exercise an informed judgment on whether to accept or reject the plan. The plan is proposed and acceptance thereof urged by a management (1) which is responsible for the company's present predicament, (2) whose interests appear to conflict with those of the investor-creditors, since the latter are being required to give up a substantial portion of their claims while the junior security holders continue to retain an interest in the business, and (3) which the Commission has accused of making false and misleading statements in soliciting acceptances of the plan (see note 3, *supra*, p. 9). There has been no investigation of the management to ascertain its capabilities and whether the

company has any claims against it; and no study of what type of reorganization of the company's businesses and finances is necessary for it to achieve economic health. These factors are among those which this Court referred to in the *General Stores* case as "typical instances where c. X affords a more adequate remedy than c. XI" (350 U.S. at 467). See, also, *Securities and Exchange Commission v. Liberty Baking Corp.*, 240 F. 2d 511 (C.A. 2), certiorari denied, 353 U.S. 930, where the court stressed a number of these factors in reversing a district court decision refusing to transfer a Chapter X proceeding.

2. The decision below also warrants review because it marks the first time that an appellate court has permitted Chapter XI to be utilized to deny public investor-creditors their right to absolute priority—a result which we believe is at variance with both *Realty* and *General Stores*. The importance of this issue is underlined by the fact that two other district courts recently have similarly approved the use of Chapter XI in situations where public investor-creditors would be denied absolute priority.¹

A plan of reorganization under Chapter X may not be confirmed unless it is "fair and equitable" (11

¹In re *Crumpton Builders, Inc.* (M.D. Fla., No. 63-42-T), appeal from order denying motion to dismiss proceedings pending *sub nom. Securities and Exchange Commission v. Crumpton Builders, Inc.*, C.A. 5, No. 20712; In re *American Guaranty Corporation* (D. R.I., No. 63B17), appeal from order denying motion to dismiss proceedings pending *sub nom. Securities and Exchange Commission v. Burton*, C.A. 1, No. 6223. The appeal in the *Crumpton* case was argued on November 20, 1963, and the appeal in the *Burton* case on December 4, 1963.

U.S.C. 621(2)). These are "words of art" and require "that in any plan of corporate reorganization unsecured creditors are entitled to priority over stockholders to the full extent of their debts and that any sealing down of the claims of creditors without some fair compensating advantage to them which is prior to the rights of stockholders is inadmissible" (*Realty case, supra*, 310 U.S. at 452). This Court has consistently required, in whatever context publicly held corporations have been reorganized, that investor-creditors must be afforded full compensatory treatment before junior interests may participate.⁶

The present plan plainly does not satisfy the "fair and equitable" standard. For here the "sealing down of the claims of creditors" through elimination of the unpaid rentals and treatment of rentals already received as if they were a return of capital was made without any "compensating advantage to them which is prior to the rights of stockholders." On the contrary, the reduction of the investor-creditors' prior claims was obviously designed to enable the junior stock interests to participate in the reorganized corporation at the creditors' expense. If the fair and

⁶See, e.g., *Northern Pacific Railway v. Boyd*, 228 U.S. 482, 502, 504 (equity receivership); *Case v. Los Angeles Lumber Co.*, 308 U.S. 106, 115-116 (reorganization under Section 77B of the Bankruptcy Act); *Consolidated Rock Products Co. v. DuBois*, 312 U.S. 510, 527-529 (reorganization under Section 77B of the Bankruptcy Act); *Ecker v. Western Pacific R. Corp.*, 318 U.S. 448, 484 (reorganization under Section 77 of the Bankruptcy Act); *Otis & Co. v. Securities and Exchange Commission*, 323 U.S. 624, 633-640 (reorganization under the Public Utility Holding Company Act of 1935).

equitable standard were applied in this case, it seems almost certain that only creditors would be entitled to any interest in the reorganized company.

Prior to 1952, Chapter XI had required that an arrangement, like a plan of reorganization under Chapter X, be "fair and equitable." That requirement was deleted from Chapter XI in that year, however (66 Stat. 433). The court of appeals was of the view that because of such deletion the fact that a plan of arrangement would not satisfy the "fair and equitable" standard is irrelevant in determining whether a Chapter XI proceeding should be transferred to Chapter X, where the standard still applies.

This conclusion is fully answered by *General Stores, supra*. That case was decided in 1956, four years after the amendment. The Court there listed, as one of three "typical instances where c. X affords a more adequate remedy than c. XI," a case where "[r]eadjustment of all or a part of the debts of an insolvent company without sacrifice by the stockholders may violate the fundamental principle of a fair and equitable plan . . . as the *United States Realty Co.* case emphasizes" (350 U.S. at 467, 466). In other words, the fact that a plan of arrangement under Chapter XI need no longer satisfy the "fair and equitable" standard may be the very reason why Chapter XI does not provide adequate relief where the interests of public creditors are being adversely affected for the benefit of junior security holders. Thus, in *Securities and Exchange Commission v. Liberty Baking Corporation*, 240 F. 2d 511, 515 (C.A.

2), certiorari denied, 353 U.S. 930, the court stated that because there was "a grave question whether the plan would deprive creditors of their 'absolute priority' rights as against stockholders * * * the need for resort to Chapter X is much greater than was the need in General Stores."

The legislative history of the deletion of the "fair and equitable" standard from Chapter XI shows that this change was a mere "clarifying" and "uncontroversial" amendment.¹ Its intent, we believe, was to make it clear that under Chapter XI trade creditors could have their claims reduced without any change in the interests of junior security holders. Cf. *Securities and Exchange Commission v. Wilcox-Gay Corp.*, 231 F. 2d 859 (C.A. 6). It is one thing if informed businessmen, in order to retain a customer who is seeking to extricate itself from financial difficulties, are willing to accept a reduction of their claims without any change in the junior security interests. It is quite another, however, if uninformed public investor-creditors are required to accept less than their claims in a reorganization in which the junior interests who propose the plan themselves participate.

Whatever discretion a district court may have in other situations in deciding whether a Chapter XI

¹ H. Rep. No. 2320, 82d Cong., 2d Sess. (1952), pp. 2-3. See also S. Rep. No. 1395, 82d Cong., 2d Sess. (1952), p. 23, containing a chart prepared by the National Bankruptcy Conference, which initiated these amendments, classifying the deletion of "fair and equitable" from Section 366 as a "perfecting or clarifying" amendment, as distinguished from a "substantive" or a "corrective" one.

proceeding belongs in Chapter X, here transfer to Chapter X was required as a matter of law. For, as we have shown, Chapter XI is not available for dealing with the interests of investor-creditors; such interests may be affected only under the "fair and equitable" standard which Chapter X alone requires.

CONCLUSION

For the foregoing reasons this petition for a writ of certiorari should be granted.

Respectfully submitted.

ARCHIBALD COX,
Solicitor General.

PHILIP A. LOOMIS, Jr.,
General Counsel,

DAVID FERBER,
Associate General Counsel,

ALLAN R. ROTH,
Attorney,
Securities and Exchange Commission.

FEBRUARY 1964.

APPENDIX A

United States Court of Appeals Tenth Circuit

Nos. 7392-7474—November Term, 1963

In the Matter of AMERICAN TRAILER RENTALS COMPANY

**SECURITIES AND EXCHANGE COMMISSION, APPELLANT
vs.**

**AMERICAN TRAILER RENTALS COMPANY, DEBTOR--
APPELLEE**

***Appeal From The United States District Court For
The District of Colorado***

**Before MURRAH, Chief Judge, and PHILLIPS and
PICKETT, Circuit Judges.**

PICKETT, Circuit Judge.

This is a consolidated appeal from two orders of the United States District Court for the District of Colorado, growing out of an arrangement proceeding under Chapter XI of the Bankruptcy Act (11 U.S.C. § 701, et seq.), in which American Trailer Rentals Company is the debtor.¹ Securities and Exchange

¹ No. 7392 is an appeal from a denial of the Commission's application under Section 328 of the Bankruptcy Act (11 U.S.C. § 728), to dismiss the debtor's petition under Chapter XI, on the ground that it should properly be a Chapter X proceeding.

No. 7474 is an appeal from an order denying the Commiss-

Commission is the appellant in both instances. The S.E.C. contends that the District Court erred in denying its motion to intervene and to dismiss the Chapter XI petition unless the proceedings were continued under Chapter X of the Bankruptcy Act. (11 U.S.C. § 501, et seq.) It is urged that the relief afforded by Chapter XI is inadequate because the circumstances disclosed by the record indicate the necessity of an independent investigation of the proposed new management and the methods used in soliciting approval of the plan, which can be accomplished only in a Chapter X proceeding.

The debtor is a Colorado corporation organized in 1958 to engage in the business of renting automobile trailers to the general public for local and cross-country trips. Originally, the trailer rental system had been operated by a complex of inter-related corporations, of which the debtor was one. In 1961, the remaining corporations of the complex were merged into the debtor. Under the rental system as operated by debtor, trailers were sold to individuals and leased back to the debtor. These trailers are the ordinary, utility type, which may be attached to the rear of an automobile by means of a detachable bumper hitch furnished as part of the trailer equipment. The trailers were placed at gasoline service stations in several states, with individual station operators acting as rental agents for the debtor.²

Under the sale-and-lease-back contracts with the individual trailer owners, the debtor had agreed to a

sion's motion to intervene in the Chapter XI proceedings to show a violation of Section 17 (fraud provisions) of the Securities Act of 1933, and confirming the arrangement as modified.

² When the petition herein was filed, these agents, scattered throughout the country, numbered about 500.

fixed return per year, based on the cost of the trailer. Three payment plans were used, (1) a guaranteed payment of 2% per month for 10 years, (2) a guaranteed payment of 3% per month for 5 years, and (3) a payment of 35% of the rental income less repairs. A majority of the agreements were for 2% per month for 10 years. The debtor, in its proposed arrangement, stated that these fixed payments, since unrelated to the actual earnings of the trailers, were the major cause of its financial difficulties.

When the petition was filed on December 20, 1962, the debtor stated its assets to be \$685,608.82, and its liabilities \$1,367,890.66. Its trailer network consisted of approximately 3,000 trailers, owned by about 1,200 individuals, and located throughout the country at the rental stations. Debtor's peak earnings had been \$60,000 per month, but diminished to about \$14,000 per month when this proceeding was instituted, and was down to \$4,000 per month when the Commission's petition was filed. Considering the payments made

? Assets:

\$500,000.00	rental network (intangible asset)
173,196.07	accounts receivable
10,712.75	furniture and equipment
1,700.00	vehicles and service equipment.

\$685,608.82

Liabilities:

\$5,611.58	secured debt (chattel mtgs. on furniture, vehicles and service equipment)
727,585.97	executory contracts
230,783.29	accounts payable
392,533.15	notes payable
6,691.97	wages and commissions
4,684.70	taxes

\$1,367,890.66

(From Referee's Statement)

under the leasing agreements as a return of capital, the trailer owners' remaining investment in the 3,000 trailers totaled \$1,532,902.43.

The arrangement proposed, as modified, provides that the trailer owners would transfer title to their trailers in exchange for one share of stock in the newly created Capitol Leasing Corporation,⁴ for each two dollars of their remaining investment in exchange for the title to the trailers, and forego their claims for past and future payments growing out of their leasing agreements. Persons who had paid in \$200,677 for trailers which were never manufactured are to receive one share for each \$2.00 paid.⁵ The trailer rental system is to be assigned to Capitol Leasing in exchange for 107,100 shares. Unsecured creditors are to receive one share for each \$3.50 of debt, except those unsecured creditors who are also officers and directors of the debtor, who are to be given one share for each \$5.50 of debt. A \$40,000 bank debt is to be assumed by the president of the debtor and he will receive one share for each \$5.50 of the assumed obli-

⁴ Capitol Leasing Corporation was formed on March 27, 1962, for the purpose of salvaging debtor's business. In May of that year, it commenced the public offering of its shares under the Regulation "A" Exemption, Securities Act of 1933, in exchange for cash or trailers. Only trailers were exchanged. On October 9, 1962, the S.E.C. stop-ordered the Regulation "A" offering on the grounds that the notification and offering circular were false and misleading. By that time, Capitol Leasing had acquired 299 trailers in exchange for 88,332 shares of its no-par stock, on the basis of one share for each \$2.00 of investment. The only outstanding shares of Capitol's authorized 3,200,000 shares are those issued in exchange for the trailers prior to the stop-order.

⁵ This amount was paid to DeMar, Inc., a Nebraska corporation, which in 1960 was granted the exclusive right to manufacture trailers for the system, but has since been adjudicated a bankrupt.

gation. The amount due the accountants is to be paid by individual officers and directors of the debtor as guarantors of debtor's note. The court expressed some objection to the initial arrangement, indicating that it did not appear to give the trailer owners a "fair shake." It was indicated that an acceptable plan should be one which resulted in the investors' control of the corporation, and noted that investors should perhaps get more than one share for each \$2.00 of investment, while management should get less than one share for each \$3.50 as was originally proposed. Following those comments, debtor submitted the amendments to the arrangement.

The Commission, in its motion under Section 328 of the Bankruptcy Act, 11 U.S.C. § 728, to dismiss the Chapter XI proceedings, alleges that this is properly a Chapter X proceeding for three reasons; first, that the debtor needs more than just an arrangement with its unsecured creditors; second, that the public investors need a disinterested trustee to protect

⁶ Title 11, U.S.C. § 728, provides:

"The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under Chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter, be filed. Upon the filing of such amended petition, or if such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter."

and enforce their rights; and third, that Chapter X is required so that public investors will receive fair and equitable treatment. Since a petition for reorganization under Chapter X cannot be filed if "adequate relief would be obtainable by a debtor's petition under * * * Chapter XI * * *." (§ 146(2), Bankruptcy Act; 11 U.S.C. § 546(2)), the ultimate question is whether "adequate relief" is obtainable under the debtor's proposed arrangement.¹ Chapter XI does not require that the arrangement be "fair and equitable" as does Chapter X, (§ 221(2), Bankruptcy Act, 11 U.S.C. § 621(2); but only that it be feasible and in the best interest of the creditors. (§ 366(2), Bankruptcy Act, 11 U.S.C. § 766(2)). The essential consideration in the choice between Chapter X and XI is "the needs to be served." *General Stores Corp. v. Shlensky*, 350 U.S. 462, 466. Although Chapter XI is limited to arrangements dealing with unsecured debts, (§ 306(1) Bankruptcy Act, 11 U.S.C. § 706(1)), the mere existence of public investors does not preclude the use of Chapter XI. *General Stores Corp. v. Shlensky*, *supra*; *Grayson-Robinson Stores, Inc. v. S.E.C.*, 2 Cir., 320 F. 2d 940. However, the more complex the debt structure and stock distribution, the greater the likelihood that the more complex procedures and safeguards of Chapter X are required. *In re Transvision*, 2 Cir., 217 F. 2d 243, cert. denied

¹ The judge may, upon application and notice, dismiss a Chapter XI petition if he finds that the proceedings should have been brought under Chapter X. (§ 328, Bankruptcy Act, 11 U.S.C. § 728). This determination rests in his sound judicial discretion. *General Stores Corp. v. Shlensky*, 350 U.S. 462; *S.E.C. v. Wilcox-Gay Corp.*, 6 Cir., 231 F. 2d 859; *In re Transvision, Inc.*, 2 Cir., 217 F. 2d 243, cert. denied 348 U.S. 952.

348 U.S. 952; Grayson-Robinson Stores, Inc. v. S.E.C., *supra*.*

The Securities Exchange Commission argues that the arrangement as proposed by debtor is not really an arrangement at all, because if the plan is effected, the creditors of the debtor will be transformed into shareholders of the new corporation. The arrangement indicates that there is an aggregate remaining capital investment in the trailers of \$1,532,902.43, which includes unpaid leasing fees in the amount of \$710,597.53. Therefore, debtor states that trailer

* Chapter X involves more complex procedures and safeguards than does Chapter XI. Chapter X requires the appointment of an independent trustee, the investigation of the activities and affairs of the debtor, the plan or reorganization as formulated by the trustee, the S.E.C. participating in an advisory capacity, and the creditors' committees subject to judicial control and scrutiny. See, generally, Collier on Bankruptcy, 14th Ed. Vol. 6, §§ 0.08[3], 0.09.

Although not expressly limited to the use of large corporations, Chapter X was, in effect, designed for the larger corporation which shares widely held by the public and with complicated debt structures. S.E.C. v. U.S. Realty Co., 310 U.S. 434. However, the choice between Chapter X and Chapter XI "is not determined solely by the size and capital structure of the company but, rather, by the nature of the interested parties, the necessity for independent investigation and control, the degree to which the debtor's activities must be readjusted." Collier on Bankruptcy, 14th Ed. Vol. 6, 1962 Supp. p. 7.

Factors appropriate to a Chapter XI arrangement include (1) simple corporate structure, (2) more than half the common stock held by management, (3) no interference with shareholder's rights, (4) acceptance of plan by unsecured creditors, (5) provision for priority creditors, (6) inability of corporation to bear expense of Chapter X proceeding. *In re Lea Fabrics*, 3 Cir., 272 F. 2d 769; vacated as moot sub. nom. S.E.C. v. Lea Fabrics, Inc., 363 U.S. 417. Collier on Bankruptcy, 14th Ed. Vol. 6, 1962 Supp. p. 7.

owners are to be compensated for their claims at the rate of one share for each \$2.00 since the plan states that 766,451 shares of Capital Leasing will be required to acquire title to all the trailers.⁹ As the S.E.C. points out, there is no provision in the arrangement for trailer owners who do not choose to exchange their trailers for stock. In such cases the owners would retain title and the right of possession to their trailers.

The Commission also infers that debtor's remarks concerning a need for additional financing in order to salvage the business, and the implication that debtor's management may have engaged in some mishandling of corporate funds, supports the position that an independent trustee such as Chapter X provides, is necessary to assure fair and equitable treatment of public investors. The S.E.C. states that the most serious aspect of unfairness relates to the compensation of debtor's shareholders, as compared to the trailer owners. The S.E.C. argues that in the absence of a fresh contribution of capital, the stock-holders are entitled to receive nothing until the creditors (the trailer owners) are compensated in full, and that to do otherwise, as the plan contemplates, would be a violation of the absolute priority rule as laid down in Case v. Los Angeles Lumber Products Co., 308 U.S. 106,¹⁰ reh. denied 308 U. S. 637. But Section 366 states in part, that "Confirmation of an arrangement shall not be refused solely because the interest

⁹ Debtor assumes that the leasing fees previously paid trailer owners constituted a return of capital, if so, trailer owners would appear to receive compensation for their claims.

¹⁰ The 1952 Amendment of § 366(2), Bankruptcy Act, 11 U.S.C. § 766(2), (66 Stat. 433, P.L. 456, 82d Cong., 2d Sess. § 35) eliminated from Chapter XI proceedings the "fair and equitable" provision, since in S.E.C. v. U.S. Realty Co., 310 U.S. 434, it was held that they were "words of art" having a

of a debtor, or if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement." In the legislative

well-understood meaning requiring an application of the principles of priority. The Court stated (310 U.S. 434, 452) that:

"The phrase signifies that the plan or arrangement must conform to the rule of *Northern Pacific Ry. Co. v. Boyd*, 228 U.S. 482, which established the principle which we recently applied in the *Los Angeles case*, [Case v. Los Angeles Lumber Products Co., 308 U.S. 106, reh. denied 308 U.S. 637] that in any plan of corporate reorganization unsecured creditors are entitled to priority over stockholders to the full extent of their debts and that any scaling down of the claims of creditors without some fair compensating advantage to them which is prior to the rights of stockholders is inadmissible."

However, Chapter XI is derived from the composition procedure of the former § 12 of the Bankruptcy Act, in which the fair and equitable rule did not apply. The essence of Chapter XI is to permit the scaling down of debts, while allowing the debtor to keep his business and property. While this may be in the best interests of the creditors, it is contrary to the principles of priority expressed in the Boyd and Los Angeles Lumber cases. But the rule of those cases "cannot realistically be applied in a Chapter XI * * * proceeding. Were it so applied, no individual debtor and, under Chapter XI, no corporate debtor where the stock ownership is substantially identical with management could effectuate an arrangement except by payment of the claims of all creditors in full." U.S. Code Cong. & Adm. News, 82d Cong. 2d Sess. Vol. 2, 1952, pp. 1981-2; Hanna & MacLachlan, *The Bankruptcy Act Annotated* Foundation Press, 1957, pp. 246-7.

But see, S.E.C. v. Liberty Baking Corp., 2 Cir., 240 F. 2d 511, cert. denied 353 U.S. 930, which indicates that the "fair and equitable" rule may be applied in determining whether Chapter X or Chapter XI should be used. If the arrangement proposed to be accomplished under Chapter XI contains features which bring it within Chapter X; then an application of the "fair and equitable" rule is relevant. However, if the plan is properly within Chapter XI, it does not have to measure up to that standard. Collier on Bankruptcy, 14 Ed. Vol. 9, § 9.18 [2.1]. Collier states that "Since the legislative elimi-

history of the 1952 amendments relating to Section 366, it is stated:

"The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the Boyd and Los Angeles cases shall not be operative under those three chapters. [Chapters XI, XII, XIII]." U.S. Code, Cong. and Adm. News, 82d Cong. 2d Seas. 1952, p. 1982.

S.E.C.'s position begs the question since it assumes that the arrangement has features which require the procedures of Chapter X. See S.E.C. v. Liberty Baking Corp., 2 Cir., 240 F. 2d 511, cert. denied 353 U.S. 930. However, since the granting of the motion rests in the discretion of the court, while we think this is a border-line case, it does not appear that the S.E.C. has shown that adequate relief is not obtainable in Chapter XI proceedings or that there has been an abuse of that discretion warranting reversal.

The second order appealed from relates to the confirmation of the arrangement as modified, and the denial of S.E.C.'s request to intervene to show violations of Section 17 (fraud provisions) of the Securities Act of 1933, (15 U.S.C. § 77q). While Securities issued under Chapter XI proceedings are exempt from Section 5 (registration) under the Securities Act of 1933, (15 U.S.C. § 77e), they are not exempt from Section 17.¹¹

nation of the 'fair and equitable' test, use and reliance on these words, in view of their past interpretation, should not be continued. While several decisions have continued to refer to the 'fair and equitable' test, other and sound reasons for favoring Chapter X over Chapter XI were present in those cases." Id. at p. 306.

¹¹ Section 3(a)(10), Securities Act of 1933, 15 U.S.C. § 77c(a)(10); Section 17(c), Securities Act of 1933, 15 U.S.C. § 77q(c); Section 393, Bankruptcy Act, 11 U.S.C. 793.

The S.E.C. alleges that at the time debtor was sending letters to the trailer owners urging them to exchange their trailers for shares of Capitol Leasing stock, the president of Capitol and the officers and directors of the debtor were withdrawing their trailers from debtor and were leasing them to another concern engaged in a similar business, and were also urging their relatives to do the same. This was not disclosed to the trailer owners, nor were trailer owners furnished information of Capitol's financial condition or its management. Trailer owners were not told of pending proceedings involving other stock fraud charges against Capitol.

The S.E.C. has on two prior occasions stopped the sale of securities by debtor and Capitol. The first was with regard to debtor in 1961 when the S.E.C. informed debtor that its trailer rental plans were investment contracts and, therefore, securities requiring registration. A registration statement was filed, but never became effective, and the issue was stop-ordered on the ground that the statement contained false and misleading statements and omitted certain material facts. The second involved the shares issued under the Regulation "A" exemption by Capitol Leasing Company in exchange for trailers. (See, footnote 4, supra.)

The S.E.C. also notes a number of other omissions of facts which it considers material if the investors are to be able to make an informed judgment on the arrangement. S.E.C. contends that the circumstances surrounding the offering of Capitol Leasing stock under the arrangement is even more unfavorable and with less disclosure than the offering of Capitol under the Regulation "A" exemption which was stop-ordered.

Under Section 17(a), Securities Act of 1933, 15 U.S.C. § 77q(a), the failure to state the whole truth with regard to a security is equally as unlawful as statements of halftruths or deliberate falsehoods. *Hughes v. S.E.C.*, C.A.D.C., 174 F. 2d 969. It is the impression created by the statements which determines whether they are misleading. *Kalwajtys v. F.T.C.*, 7 Cir., 237 F. 2d 654, cert. denied 352 U.S. 1025; *S.E.C. v. Macon*, D.C. Colo., 28 F. Supp. 127. Cf. *Birko v. S.E.C.*, 2 Cir., 316 F. 2d 137. Section 17(a) is not limited to the common-law definition of fraud. *Hughes v. S.E.C.*, *supra*; *Norris & Hirshberg v. S.E.C.*, C.A.D.C., 177 F. 2d 228, cert. denied 333 U.S. 867; *Loss*, Securities Regulation, 1 Vol. Ed. p. 1435. From the authorities, it appears that if the stock involved here were not part of an arrangement, the disclosures made with regard to it would be clearly inadequate. No authority has been found which would indicate that recipients of stock issued in connection with an arrangement are not entitled to as much information as are those persons acquiring stock under ordinary conditions.

The S.E.C. points out in its brief that the simplest procedure would be for debtor to voluntarily provide the needed information,¹² and, failing in that, the referee should have ordered that disclosure be made. We think this is a matter which the District Court

¹² In its brief, the S.E.C. states:

"It has been the Commission's position throughout that the simplest and most efficient resolution of the issue it has raised would be for the debtor and Capitol to send to trailer owners a statement or letter containing the material facts to which they are entitled. Had this been done, there would have been no need for this appeal or the expensive and time-consuming antecedent proceedings. Trailer owners could have been resolicited to accept the arrangement on the basis of adequate and accurate information."

can now handle. If it appears that, for the protection of those being solicited to accept the plan, additional information is necessary, the Court should so order. The Court has directed that the stock ratio for Capitol Leasing be such that the creditors will have control of the new corporation. In proceedings such as this, the District Court retains jurisdiction until the plan is carried out. §§ 368, 369, Bankruptcy Act, 11 U.S.C. §§ 768, 769. It may be that even without the additional information, the arrangement would still be in the "best interests of the creditors" (§ 366, 11 U.S.C. § 766), since that involves a comparison between what they will receive under the arrangement and what they would receive on liquidation. *In re Village Men's Shops, Inc.*, D.C. Ind., 186 F. Supp. 125. The debtor has little or no tangible assets, and if it were liquidated it is not unlikely that the trailer owners, or at least many of them, would have difficulty realizing anything for their trailers.¹³

For an arrangement to be "feasible," the creditors must be assured of receiving what is promised them under the arrangement, but it does not require an assurance of future business success. *In re Slumberland Bedding Co.*, D.C. Md., 115 F. Supp. 39.

Affirmed.

¹³ In the debtor's proposed arrangement it was stated: "Unless the plan is adopted, proponents suggest that creditors will receive little, if anything, in settlement of debtor's obligation to them, and that trailer owners may find themselves unable to realize any value for their trailers or any income from their operation."

APPENDIX B

In the United States District Court for the District
of Colorado

Br. 33276

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, DEBTOR.

OFFICIAL TRANSCRIPT

Ruling of the Court

Proceedings had before the Honorable Alfred A. Arraj, Chief Judge, United States District Court for the District of Colorado, beginning at 9:00 a.m., on the 3d day of May, 1963, in Court Room A, Main Post Office Building, Denver, Colorado.

Ruling of the Court

The COURT: The Court is of the opinion that the Securities and Exchange Commission has failed to establish that the findings of fact and conclusions of law of the Special Master with the exception of those findings related to the cost are clearly erroneous.

Therefore, the Court will confirm and adopt the findings insofar as they pertain to the denial of the 328 motion.

As I stated at the outset of this hearing, I have studied the file in this case prior to the hearing. I listened to the arguments of counsel, and I am not convinced that the needs to be served here can best be met by a Chapter 10.

The cases that were cited and which I looked at, none of them involved a company who operated a business such as the one that we have here. It seems to me that actually there are no assets whatsoever in this corporation, except maybe some desks, some furniture, except its net worth, if we may use that term, or—I think that's satisfactory—its net worth of filling-station operators who serve as agents to rent these trailers out to prospective users.

Now, there may be in this situation need for new management, and there certainly is some question in my mind as to whether or not the management that is presently representing it would—I mean, operating it, would continue to do so for the best interests of the investors. However, that has not been clearly established yet and if there is any indication of any criminal activity on the part of the people who are running the company, this should by the SEC be investigated and if found that there is any or has been any criminal activity should be reported to the proper authorities in the Justice Department.

I don't think it is the function of this Court under a Chapter 10 proceedings to—that is, the primary function—to investigate a claim of poor business management or improper business management, or maybe even criminal action on the part of management or some officers or directors of the company. This would be—this investigation would be incidental.

I do not think the investigation can be best made by a trustee, because there are no funds with which to do this. Now, there are some funds coming in, but these funds better be used to pay the debts of the corporation, and to pay off the investors if there is sufficient funds.

It has been our experience—shall I say, my experience, in this Court, with the exception of one case

under Chapter 10 that I have had, none of them work out. We spend a good bit of the money that is available on trustees and attorneys fees and we end up in worse shape than we did before.

Most of these businesses that reach this point probably would be better off to be in bankruptcy as far as the creditors are concerned. In other words, they are ill. The illness is terminal and it is just a question of whether or not the life should be prolonged, I think aptly describes the situation that we find in many of these cases.

Now, I have, or, I want to express for the record some objection to the proposed plan. I do not think that the proposed plan gives the owners of the trailers a fair shake.

In other words, unless this plan that is finally determined in this case under the Chapter 11 is such a plan that the investors themselves will have control of this corporation and not the management who get it in this shape, then I say it will be an improper plan. Therefore, that would suggest that the investors should have more than one share of stock for each two dollars and management less than one share for each three dollars and a half, but at any rate, the proportion of the ratio should be such as the investors will have control of the corporation. This is the only way, in my opinion, that it can properly operate.

Now, also in connection with the plan, consideration should be given to treating all creditors alike. One creditor should not be paid just because the officers guaranteed that payment and another creditor not paid in cash. The bank, for example. These people are knowledgeable in this business. They are sophisticated lenders, and to treat them with some special treatment as against an individual who is a creditor is not, in my opinion, equity or justice.

Now, there is still pending, as I understand it, the motion of the SEC to intervene. This is a matter to be determined by the referee, but it seems to me the SEC could very well serve a useful purpose in a Chapter 11 proceedings. They have certain expertise in the field of securities. They have certain knowledge that would be helpful. They can advise and they can also serve somewhat in a similar capacity as they do under Chapter 10. I merely pass that on for what it may be worth.

I think under the circumstances here that Chapter 11 having been first filed and the rules as I understand it that Chapter 10 should be used only if 11 is not available, which gives further weight to the conclusion that the findings of the referee are not clearly erroneous, because I think Chapter 11 is available in the state of the matter as it is presented to the Court at this time.

* * * * *

Either counsel have anything further at this time?

Mr. MAXWELL: [counsel for the debtor] May I make one comment?

The COURT: Yes.

Mr. MAXWELL: I agree with some of the comments you made on the alterations on the plan and such will be presented along the line that you have suggested.

The COURT: Thank you, Mr. Maxwell. You may announce recess.

APPENDIX C

In the United States Court of Appeals for the Tenth
Judicial Circuit Sitting at Denver, Colorado

TWENTY-FIRST DAY, NOVEMBER TERM, MONDAY, DECEMBER 9TH, 1963

Present: Honorable JEAN S. BREITENSTEIN, Circuit
Judge, and other officers as noted on the 12th day of
November, 1963.

Before Honorable ALFRED P. MURRAH, Chief Judge,
and Honorable ORIE L. PHILLIPS and Honorable
JOHN C. PICKETT, Circuit Judges.

SECURITIES AND EXCHANGE COMMISSION, APPELLANT,

7392-7474

vs.

AMERICAN TRAILER RENTALS COMPANY, APPELLEE.

In the Matter of

AMERICAN TRAILER RENTALS COMPANY, DEBTOR

*Appeals from the United States District Court for the
District of Colorado.*

These causes came on to be heard on the transcript
of the record from the United States District Court
for the District of Colorado and were argued by
counsel.

On consideration whereof, it is ordered and adjudged by this court that the judgment of the said district court in these causes be and the same is hereby affirmed.

A true copy as of record,

Teste:

ROBERT B. CARTWRIGHT,
Clerk.

Office-Supreme Court, U.S.

FILED

MAR 9 1964

JOHN F. DAVIS, CLERK

LIBRARY
U. S. CIRCUIT COURT
IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1964

No. 888 35

SECURITIES AND EXCHANGE COMMISSION,

Petitioner,

v.

AMERICAN TRAILER RENTALS COMPANY,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

ARTHUR W. BURKE, JR.

Of Counsel.

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Attorney for Respondent

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IN THE
**SUPREME COURT
OF THE UNITED STATES**

October Term, 1963

No. 828

**SECURITIES AND EXCHANGE COMMISSION,
Petitioner,**

v.

**AMERICAN TRAILER RENTALS COMPANY,
Respondent.**

**BRIEF IN OPPOSITION TO PETITION FOR A WRIT
OF CERTIORARI TO THE UNITED STATES COURT
OF APPEALS FOR THE TENTH CIRCUIT.**

Respondent, American Trailer Rentals Company, herein sets forth grounds why the above-entitled cause should not be reviewed by this Court and urges that the Petition of the Securities and Exchange Commission for a Writ of Certiorari be denied.

OPINIONS OF COURTS BELOW

The opinion of the Court of Appeals is reported in 325 F.2d 47. The oral ruling of the District Court is not reported.

JURISDICTION

The jurisdiction of this Court is invoked, under 28 U.S.C. 1254 (1).

QUESTION

The petitioner has set forth as the question presented: (Petition, p. 2)

"Whether a corporate rehabilitation under the Bankruptcy Act, affecting the rights of widespread public investor-creditors, including a scaling down of their claims for the benefit of stockholders, may be conducted under Chapter XI of the Bankruptcy Act or whether transfer to Chapter X is required."

REASONS FOR DENYING THE PETITION

1. This Court has previously 'settled' the question posed by petitioner.
2. The opinion of the court of appeals does not conflict in principle with any other decision of any other court of appeals.
3. The opinion of the court of appeals does not conflict with the teachings of this Court.

It is well to point out that the question, as set forth by the petitioner, assumes facts which are not true. There was, in fact, a substantial sacrifice of equity position by the stockholders. Further, certain stockholders are substantial general creditors and these have accepted one share of stock for every \$5.50 of debt as against one share of stock for every \$2 of trailer owners. The total shares of stock to be issued to such stockholders will be insubstantial in number, carry restrictions of dividends and liquidation rights for five years and are permitted only one vote for every seven shares of stock.

THIS COURT HAS PREVIOUSLY SETTLED THE QUESTION POSED BY PETITIONER

A reading of two of the leading cases on the subject readily reveals that, contrary to the position of petitioner, this question has been settled by this Court. In *Securities and Exchange Commission v. United States Realty and Improvement Company*, 310 U.S. 434, and *General Stores Corp. v. Shlensky*, 350 U.S. 462, this Court determined that the presence of any particular capital structure or particular creditor may be factors to be considered in determining the ability of Chapter XI (as opposed to Chapter X) to "meet the needs to be served", but they are only factors and not a controlling standard. In the exercise of its discretion, the lower court must determine the ability of either Chapter to meet the standard, which standard is fulfilling "the needs to be served". This has clearly been established by this Court.

General Stores Corporation v. Shlensky, *supra*:

"The character of the debtor is not the controlling consideration in a choice between Ch X and Ch XI. Nor is the nature of the capital structure. It may well be that in most cases where the debtor's securities are publicly held Ch X will afford the more appropriate remedy. But that is not necessarily so. A large company with publicly held securities may have as much need for a simple composition of unsecured debts as a smaller company. And there is no reason we can see why Ch XI may not serve that end. The essential difference is not between the small company and the large company but between the needs to be served."

As to the specific question propounded by the petitioner, this Court has answered that question first in the

U. S. Realty case, *supra*. United States Realty was a New Jersey corporation with 900,000 shares outstanding, 7,000 shareholders, listed on the New York Stock Exchange, liabilities of \$5,051,416, current liabilities of \$74,916, two series of public debentures, the first of \$2,339,000 and the second of \$3,000,000, and was the guarantor on \$3,710,500 of public held mortgage certificates. This Court, in decision on that case held:

... we find in neither chapter any definition or classification which would enable us to say that a corporation is small or large, its security holders few or many or that its securities are held by the public so as to place the corporation exclusively within the jurisdiction of the court under one chapter rather than the other. But granting the jurisdiction of the court

This Court then went forward with an explanation why Chapter XI did not meet the needs to be served. In the same case (p. 455) this Court stated:

"A bankruptcy court is a court of equity, . . . A court of equity may in its discretion in the exercise of the jurisdiction committed to it grant or deny relief . . ."

The teaching of the *U. S. Realty* case was enlarged in the *General Stores* case, *supra*.

General Stores Corp. v. Shlensky, *supra*:

Much of the argument has been devoted to the meaning of *Securities & Exch. Com. v. United States Realty & Improv. Co.*, 310 U.S. 434, 84 L. ed 1293, 60 S. Ct 4044. In that case we held that relief was not properly sought under Ch. XI but that Ch. X offered the ap-

propriate relief. That was a case of a debtor with publicly owned debentures, publicly owned mortgage certificates, and publicly owned stock. An arrangement was proposed that would leave the debentures and stock unaffected and extend the certificates and reduce the interest. It was argued in that case, as it has been in the instant one, that Ch X affords the relief for corporations whose securities are publicly owned, while Ch XI is available to debtors whose stock is closely held; that Ch X is designed for the large corporation, Ch XI for the smaller ones; that it is the character of the debtor that determines whether Ch X or Ch XI affords the appropriate remedy. We did not adopt that distinction in the United States Realty case. Rather we emphasized the need to determine on the facts of the case whether the formulation of a plan under the control of the debtor, as provided for by Ch XI and the other protective provisions of that chapter, would better serve the public and private interests concerned including those of the debtor.³¹⁰ U.S. at 455.

Later, in the same case this Court found:

"We could reverse them [the lower courts] only if their exercise of discretion transcended the allowable bounds."

Clearly, this Court has answered the question set forth by petitioner. The answer is that the lower court, in the exercise of its discretion, must determine whether a Chapter XI "meets the needs to be served".

THE OPINION OF THE COURT OF APPEALS DOES 'NOT CONFLICT IN PRINCIPLE WITH ANY OTHER DECISION BY ANY OTHER COURT OF APPEALS'

The petitioner states that the instant case is in conflict with a case decided in 1957 in the Second Circuit, *Securities and Exchange Commission v. Liberty Baking Corporation*, 240 F.2d 511. An examination of that case indicates that the factual situation is considerably different. Significant differences as found in the facts in the *Liberty Baking* case: the debenture holders were entitled to take over management for default on the debentures and the arrangement delayed that potential take-over for eight years, (in the instant case, the management is guaranteed to the trailer owners); the debenture holders were restricted in dividend and liquidation rights (in the instant case, the stockholder-creditors are the persons whose dividend, liquidation and even voting rights are restricted).

The *Liberty Baking* case contains some seemingly strong language but an overall reading of the case reaches the inescapable conclusion that the court of appeals, exercising the discretion referred to in *General Stores*, supra, determined that the needs to be served were not met in that particular case. Of interest is the fact that, since that determination, a further decision by the same circuit has been made by the court of appeals, in which the court determined, on appeal by the Securities and Exchange Commission, that a Chapter XI proceeding is to be measured by its ability to meet the needs to be served:

>*Grayson Robinson Stores, Inc., v. Securities and Exchange Commission*, 320 F.2d 940.

"In such circumstances a court can hardly ignore a substantially uncontradicted factual showing that

Chapter XI affords some hope of paying off creditors whereas Chapter X offers none."

In each of the foregoing cases, the second circuit court of appeals made a determination of which chapter met the needs to be served. This is the standard established by this Court, the standard applied by the second circuit and the standard applied in the instant case.

Appendix B Petition, Oral Ruling of District Court,
p. 14a:

"As I stated at the outset of this hearing, I have studied the file in this case prior to the hearing. I listened to the arguments of counsel, and I am not convinced that the needs to be served here can best be met by a Chapter X."

THE OPINION OF THE COURT OF APPEALS DOES NOT CONFLICT WITH THE TEACHING OF THIS COURT

Here the position of petitioner is overcome by the law under the first point in this brief. However, certain matters may be beneficially pointed up here:

Petitioner assumes the arrangement to be for the benefit of stockholders as against trailer owners. As previously shown, this is not true; quite the contrary. However, assuming arguendo, that this were true, that is, that stockholders were retaining their position and creditors reducing theirs, petitioner overlooks the provisions of Chapter XI itself. The plan does not have to be fair and equitable (i.e. give absolute priority to creditors over stockholders); U.S.C.A., Bankruptcy, 11 U.S.C. §766 (Amendment 1952):

"The Court shall confirm an arrangement if satisfied that —

- (1) The provisions of this chapter have been complied with;
- (2) It is for the best interests of the creditors and is feasible;"

and confirmation of the plan may not be refused solely because the interests of the stockholders will be preserved: U.S.C.A., Bankruptcy, *supra*:

"Confirmation of an arrangement shall not be refused solely because the interest of a debtor, or if the debtor is a corporation, the interest of its stockholders or members will be preserved under the arrangement."

(These two amendments were adopted July 7, 1952)

That Congress knew exactly the import and intent of these two amendments is shown in the legislative history of the 1952 amendments relating to Section 366:

"The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the *Boyd* and *Los Angeles* cases shall not be operative under those three chapters (Chapters XI, XII, XIII)." U.S. Code, Cong. and Adm. News, 82d Cong. 2nd Sess. 1952, p. 1982.

This Court has said:

Securities and Exchange Commission v. United States Realty and Improvement Co., *supra*, 310 U.S. at 455:

"Obviously the adequacy of the relief under chapter XI must be appraised in comparison with that to be

had under chapter X, and in the light of its effect on all the public and private interests concerned, including those of the debtor."

and again,

General Stores Corp. v. Schlensky, supra, 350 U.S. at 465:

"The essential difference is not between the small company and the large company but between the needs to be served."

The lower courts examined the arrangement and heard the evidence including: two days of testimony which included efforts of the Commission to establish mismanagement,² the estimate of management owning 3% to 5% of the outstanding stock (for which stockholder creditors will vote only one out of seven shares), the need for speed and economy essential in this case due to the mobility of the trailers and loss from theft, foreclosure of storage liens, or negligence by station operators, the necessity for large public liability insurance, and the voluntary release by the Company of trailers to the owners (which releases now number approximately 4,000 out of a total number of 5,866), evidencing a lack of pressure to accept the arrangement, among other things. After argument by the Securities and Exchange Commission before the Special Master, the presiding District Judge and the three senior judges (Chief Judge and two Circuit Judges) all were in agreement that Chapter X did not meet the needs to be

²The petition of the Securities and Exchange Commission refers to a petition which it filed to intervene to show violation of the anti-fraud provisions of the Securities Act of 1933; the petition should, among other things, have pointed out that there was a hearing upon the merits of the petition, and the allegations therein contained, and following that hearing, the petition was dismissed as not proven.

served. This determination was within the framework of the provisions of Chapter XI, in harmony with the pronouncements of this Court, and does not conflict with any other circuit.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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In the Supreme Court of the United States
OCTOBER TERM, 1964

No. 35

SECURITIES AND EXCHANGE COMMISSION,
PETITIONER

v.

AMERICAN TRAILER RENTALS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE
COMMISSION

OPINIONS BELOW

The oral ruling of the district court (R. 144-148) is unreported. The opinion of the court of appeals (R. 151-161) is reported at 325 F.2d 47.

JURISDICTION

The judgment of the court of appeals was entered on December 9, 1963 (R. 161-162). The petition

for a writ of certiorari was filed on February 12, 1964 and was granted on March 23, 1964 (R. 162, 376 U.S. 948). The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a corporate rehabilitation under the Bankruptcy Act, readjusting the rights of widespread public investor-creditors and scaling down their claims for the benefit of stockholders, may be conducted under Chapter XI of the Bankruptcy Act or whether transfer to Chapter X is required.

STATUTES INVOLVED

Chapters X and XI of the Bankruptcy Act (11 U.S.C. 501, *et seq.*, and 701, *et seq.*) are involved in this proceeding substantially in their entirety. The following sections are particularly pertinent:

Section 216(1) of Chapter X (11 U.S.C. 616(1)):

A plan of reorganization under this chapter—

(1) shall include in respect to creditors generally or some class of them, secured or unsecured, and may include in respect to stockholders generally or some class of them, provisions altering or modifying their rights, either through the issuance of new securities of any character or otherwise;

Section 306 (1) of Chapter XI (11 U.S.C. 706 (1)):

For the purposes of this chapter, unless inconsistent with the context—

(1) "arrangement" shall mean any plan of a debtor for the settlement, satisfaction, or extension of the time of payment of his unsecured debts, upon any terms;

Section 328 of Chapter XI (11 U.S.C. 728):

The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter; be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter.

A comparative summary of the pertinent provisions of both chapters is set forth in the Appendix, *infra*, pp. 56-58.

STATEMENT

The issue in this case is whether proceedings for the financial rehabilitation of respondent American Trailer Rentals Company ("the debtor") must be conducted as a corporate reorganization under Chapter X of the Bankruptcy Act rather than as an arrangement of its unsecured debts under Chapter XI of that Act. The issue arises out of the district court's denial of a motion by the Securities and Exchange Commission to dismiss the Chapter XI proceedings, and thus in effect to transfer the proceedings to Chapter X. The motion was made under Section 328 of the Bankruptcy Act, which provides for dismissal of a Chapter XI proceeding if the district judge finds that it "should have been brought under chapter 10 * * *."

A. THE DEBTOR'S ORGANIZATION, OPERATIONS, AND HISTORY OF FINANCIAL DIFFICULTIES.

1. The debtor was organized in 1958 as one of a group of interrelated corporations formed to engage in the automobile-trailer rental business (R. 3, 24, 32). The trailers are of the general utility type that are attached to the rear bumpers of automobiles (R. 3, 29). They are kept at gasoline stations, the operators of which act as rental agents for the debtor (R. 3, 29). The debtor had about 700 such service station agents in December 1961 (R. 22, 24), although the number had declined to about 500 by the time the petition for arrangement was filed a year later (R. 1, 3).

The business was financed largely through the sale of trailers to investors and their simultaneous lease-back. The debtor purchased most of the trailers from an affiliated corporation and placed them with the station operators for rental to the public without the investors ever having seen them (R. 3, 4, 29, 84). From 1959 through 1961 hundreds of investors throughout the Western States purchased and leased back 5,866 trailers, paying an aggregate price of \$3,587,439 (R. 3, 26, 31, 32, 66-72, 131-132). Under most of the lease-back arrangements, the trailer owners were to receive a fixed percentage of the purchase price of the trailers—either 2 percent per month for 10 years (under which terms a majority of the trailers were leased back) or 3 percent per month for 5 years (R. 3-4, 32, 98, 132). In a comparatively small number of instances the owners were to receive 35 percent of the rental income (less repair costs) produced by their trailers (R. 4, 32).

Under an agreement made with the debtor in 1960, DeMar, Inc., an affiliated corporation, was given the exclusive right to manufacture the trailers used in the debtor's system (R. 27-28, 64, 67-68). DeMar, which had no other trailer customers (R. 67), manufactured about 90 percent of the total number of trailers in the system (R. 78). Executive Sales Company, another affiliated company, operated through selling agents to sell trailers to members of the public and to arrange for the purchasers to lease their trailers to other affiliated corporations engaged in the trailer-rental business and received a commission on all trailers sold through it. (R.

32, 72, 76, 91). There were a number of these rental corporations, organized in different States, and a purchaser would lease his trailer to the one in his State (R. 68-69, 72-73, 77, 84). The debtor's functions were to maintain the network of service station rental agents, to service and maintain the trailers, to collect the rental fees and to make the payment to trailer owners required under the leasing agreements (R. 24, 30-31, 69). This entire system operated under common control or management. In 1961 Executive Sales and the individual state trailer rental corporations were merged into the debtor (R. 32, 77, 98, 125).

Executive Sales and the debtor were organized by the same people (R. 32, 61-62) and operated by a common management (R. 44).

I. H. Peters was executive vice president and a director of the debtor, an officer of Executive Sales, an officer of two or more state rental corporations, and a director of DeMar (R. 37, 60-62, 64). Peters arranged the exclusive trailer manufacturing agreement between DeMar and debtor while he was a member of the management of each company, and was compensated by DeMar for this service (R. 67-68). While an officer of the debtor, Peters received individually or through corporations under his control commissions on the majority of the trailers sold (R. 119).

W. N. Marks was president and controlling shareholder of DeMar, a director of debtor, and held irrevocable proxies to more than 141,000 shares (slightly over 32 percent) of debtor's stock (R. 28, 36, 65-66). Marks was a director of debtor when debtor entered into the exclusive trailer manufacturing agreement with DeMar (R. 61-66).

DeMar had an option for an undetermined time to purchase 50,000 shares of debtor's stock at \$1.00 per share (R. 39). Clark Hammond was an officer and a director of debtor and an officer in two of the state rental corporations (R. 37-38).

In 1961, after the Securities and Exchange Commission had informed the debtor that the sale and lease-back of the trailers under the foregoing arrangements involved investment contracts and therefore constituted securities required to be registered under the Securities Act of 1933, the debtor discontinued sales of the trailers (R. 33, 47, 84-85). Later in 1961, the debtor filed with the Commission a registration statement covering a proposed offering of such trailer sales and lease-back arrangements (R. 22-51). This registration never became effective (R. 90); instead, in November, 1962, the Commission instituted stop-order proceedings under Section 8(d) of the Securities Act of 1933 (15 U.S.C. 77h(d)), charging that the proposed prospectus contained untrue and misleading statements (R. 10-16). The debtor subsequently consented to the entry of a stop order (R. 17-18, 81-82, 84).

DeMar, which had not been merged with the debtor, filed a petition in bankruptcy after the debtor stopped buying trailers from it in 1961. The debtor had paid DeMar approximately \$200,000 for trailers that were never manufactured (R. 4, 64, 67) and an additional \$140,000-\$150,000 for trailers which were manufactured but never delivered. DeMar had mortgaged the latter trailers to a third party who took possession upon DeMar's bankruptcy (R. 109, 129).

2. Throughout its history, the debtor has never operated at a profit (R. 80). For the three years end-

² On June 11, 1963, the Commission entered its findings, opinion and stop order. Securities Act Release No. 4615.

ing September 30, 1961, it had an aggregate income from "gross rentals" of \$395,610. In the same period, the debtor made rental payments to trailer owners of \$613,021; made payments to station operators of \$118,400; and incurred additional "operating expenses" of \$668,698. The debtor's business activities during the period resulted in a "net loss" of \$504,857, exclusive of special loss items totaling \$291,976, which consisted largely of "write off[s] of accounts receivable from former affiliated companies." (R. 31.)³

The \$613,021 paid to trailer owners included payments to investors whose trailers had not yet been obtained and put into the system. They also included payments pursuant to certain of the "35-percent-of-gross-income" contracts which exceeded 35 percent of actual rental receipts from the trailers involved. (R. 46). In order to make these various payments, the debtor not only borrowed money from its officers, directors, and large stockholders (R. 4, 6, 90-91; see also R. 36, 45, 48), but also borrowed from Executive Sales money which the latter had obtained as commissions on trailer sales (R. 76, 91-92). The debtor thus used funds from the sales of additional trailers to meet its obligations to existing trailer owners. Many of the trailers proved to be de-

³ These sums are computed from figures set forth in the Summary of Operations in the debtor's registration statement filed in 1961 (R. 30-31). The debtor's auditors stated therein that they were unable to verify the expense items or to express an "overall opinion as to the combined statement of operation" (R. 41).

fective in design or otherwise unsuitable for rental. (R. 33, 50, 128). In June, 1961, some 100 trailers were unlocatable and considered lost (R. 46).⁴ The debtor also had delivery, promotional, and advertising problems (R. 69).

Prior to November, 1960, at least \$140,000, and possibly more, received by Executive Sales from public investors for the purchase of trailers had apparently been misappropriated by members of management (R. 63-64, 76-77, 122-125).⁵ Executive Sales was nevertheless obligated to pay DeMar for these trailers, and the debtor assumed this obligation when it merged with Executive Sales (R. 76, 125). Debtor's executive vice president attributed the liability for the sums taken from the debtor "almost com-

⁴ Despite the debtor's obligation under the lease-back arrangements to provide insurance adequate to compensate the trailer owners in the event of theft, damage, or destruction of trailers, the debtor had failed to maintain such insurance (R. 46).

⁵ Debtor's executive vice president, I. H. Peters, testified before the Special Master that he thought the amount was about \$141,000 (R. 124). In the prospectus filed with the Commission, debtor stated (R. 45-46) :

Prior to November, 1960, certain amounts received for trailers were not expended to purchase trailers. In an agreement dated November 17, 1960, De-Mar, Inc., agreed to manufacturer [sic] all but 57 of these trailers at a cost of approximately \$220,000. In September, 1961, De-Mar, Inc. accepted an order for an additional seventeen trailers.

On or about October 4, 1961, Executive Sales Company consummated a purchase agreement with another manufacturer for the residual forty trailers. Funds were placed in escrow on or about October 12, 1961, to cover the purchase price of these forty trailers.

pletely" to a deceased member of the original management group (R. 122, 125), but did not feel "qualified to make [the] judgment" that the two remaining members of that group, including one who owned over 15 percent of the debtor's common stock, could be held financially liable for the mismanagement (R. 38-39, 123).

In sum, the debtor received at least \$3,590,168 from public investors pursuant to trailer sale and lease-back agreements, but only about 65 percent of that amount, or \$2,339,912, had been applied toward acquisition of trailers (R. 31).⁶ Of the money the debtor actually paid to acquire trailers, 90 percent or more went to DeMar, the manufacturing affiliate in which certain of the debtor's insiders had an interest (R. 78; and see note 1, *supra*, p. 6).

3. In March 1962, after the debtor had failed in its attempt to register the sale and lease-back agreements (see *supra*, p. 7), I. H. Peters, its executive vice president, and several other persons organized Capitol Leasing Corporation ("Capitol") (R. 5, 78, 93-94). Capitol offered to exchange its stock for trailers on the basis of one share of stock for each \$2.00 that purchasers had paid for the trailers (R. 5). After Capitol had acquired 299 of the trailers in exchange for stock, the Commission temporarily sus-

⁶ It appears that two separate sales commissions were taken out of the amounts paid by public investors—one of 20 percent by one of I. H. Peters' companies and another generally ranging from 10 to 17 percent by Executive Sales (R. 74-75, 119).

88,332 shares of stock of Capitol were exchanged for trailers having "an original cost" of \$176,666 (R. 5, 95).

pended the exemption from registration upon which Capitol had relied in making this offer, on the ground that there was reasonable cause to believe that the material used in making the offer contained false and misleading statements (R. 19-21, 154).⁸

B. THE CHAPTER XI PROCEEDINGS.

On December 20, 1962, the debtor filed in the United States District Court for the District of Colorado a petition for and a proposed plan of arrangement under Chapter XI of the Bankruptcy Act (R. 1-8). It stated that its total assets were \$685,608, of which \$500,000 represented the value of its trailer rental system, *i.e.*, its arrangements with the service station operator agents (R. 137-138).⁹ Its stated liabilities were \$1,367,890, of which \$710,597 was owed to trailer owners under their leasing agreements and \$200,677 was owed to investors who had paid for but had not received trailers (R. 4, 137-138). Of the remaining claims, trade and general creditors had claims of \$71,805, officers and directors had

⁸ Capitol had relied upon the conditional exemption from registration provided for small issues under Regulation A (17 CFR 230.251, *et seq.*), pursuant to Section 3(a) of the Securities Act of 1933 (15 U.S.C. 77c (a)) (R. 79).

⁹ While the proposed plan of arrangement stated that the station rental system (which then consisted of arrangements with some 500 service station operator agents) "was built by the debtor at an estimated cost of \$500,000" (R. 3, 5), the debtor's balance sheet in 1961 showed the cost of establishing a system of 700 stations as \$33,750 (R. 42, 45). The debtor also estimated in 1961 that the cost of establishing an additional 800 rental stations would be \$56,000 (R. 28).

claims for loans to the corporation of \$285,277, an accounting firm was owed \$15,557, and there was an outstanding bank loan of \$40,000 (R. 4).

Under the proposed arrangement, trailer owners are to sell their trailers to Capitol in exchange for Capitol's stock (R. 4-5). They are to receive one share for every \$2.00 of "remaining capital investment in the trailers," which is to be determined by deducting from the original purchase price of the trailer the amount which the owners had received as rental payments (R. 4-6).¹⁰ No additional compensation to the owners is provided for the \$710,597 of unpaid rentals (R. 4-5). Owners who elect not to exchange their trailers for Capitol's stock receive nothing under the plan (R. 4-7). Investors who paid for but had not received trailers will receive one share of stock for each \$2.00 of the purchase price (R. 6). Trade and general creditors are to receive one share of stock for each \$3.50 of their claims (R. 6).

The plan of arrangement provides that the debtor will transfer its system (which it states was built at a cost of \$500,000) to Capitol in exchange for 107,000 shares, which the debtor will then distribute to its stockholders (R. 5, 7). More than 60 percent of the debtor's stock is held by eight men; seven of them are officers and directors and the eighth is one

¹⁰ This is less than the exchange that Capitol had offered some months earlier under the exemption from registration which had been suspended, since there trailer owners had been offered one share of stock for each \$2 that they had paid with no deductions for so-called "return of capital." See *supra*, p. 10.

of the original promoters of the venture (R. 37-39). The plan further provides that officers and directors will receive one share of Capitol stock for each \$5.50 of their claims for loans to the debtor, and that for five years such stock will have limited voting, dividend and liquidation rights (R. 148-150).¹¹

C. THE MOTION TO TRANSFER THE PROCEEDINGS
TO CHAPTER X.

On February 20, 1963, the Securities and Exchange Commission filed a motion under Section 328 of the Bankruptcy Act to dismiss the Chapter XI proceedings on the ground that the "proceedings should have been originally brought under Chapter X of the Bankruptcy Act because the Debtor's circumstances and capital structure are such that the relief afforded by Chapter XI is inadequate to satisfy the needs to be served." * * * (R. 8-9).

The motion was referred to a referee in bankruptcy as special master for hearing and report (R.

¹¹ The plan originally provided that officers and directors would receive one share for each \$3.50 of their claims (R. 6). When the district judge denied the Commission's motion to dismiss the proceedings (see below), he further stated (R. 146) that "I do not think that the proposed plan gives the owners of the trailers a fair shake. In other words, unless this plan that is finally determined in this case under the Chapter 11 is such a plan that the investors themselves will have control of this corporation and not the management who got it in this shape, then I say it will be an improper plan." The debtor then modified the plan to reduce the participation of its officers and directors from one share for each \$3.50 of their claims to one share for each \$5.50, and also to change the method for discharge of the debtor's bank loan and its indebtedness for accounting services (R. 148-150).

51-52). After hearing, he recommended that the motion be denied, on the ground that the Commission had not demonstrated that adequate relief was unobtainable under Chapter XI (R. 133-137), and that final "determination of the Section 328 motion ought to be postponed to the confirmation hearing [on the arrangement]" (R. 135). The district court confirmed and adopted the special master's findings and denied the Commission's motion (R. 143-144). The court stated that it was "not convinced that the needs to be served here can best be met by a Chapter 10"; and that although "there may be in this situation need for new management, and there certainly is some question in my mind as to whether or not the management that is presently * * * operating it, would continue to do so for the best interests of the investors * * * that has not been clearly established yet * * *." (R. 145).

The court of appeals affirmed. It held that "since the granting of the motion rests in the discretion of the court, while we think this is a border-line case, it does not appear that the S.E.C. has shown that adequate relief is not obtainable in Chapter XI proceedings or that there has been an abuse of that discretion warranting reversal."¹²

¹² The Commission had also filed a petition to intervene in the Chapter XI proceeding to show that, in violation of the anti-fraud provisions of the Securities Act of 1933, the information which the debtor used in procuring acceptances of the plan of arrangement was false and misleading (Tr. 323-352). As the court of appeals explained (R. 159), the Commission alleged, among other things, that "at the time debtor was sending letters to the trailer owners urging them to exchange

SUMMARY OF ARGUMENT

Section 328 of the Bankruptcy Act directs the district judge, upon the application of the Securities and Exchange Commission or of any party in interest, to transfer a proceeding under Chapter XI of the Bankruptcy Act to Chapter X "if he finds that the proceedings should have been brought under" the latter chapter. Chapter XI is not properly invoked "where c. X affords a more adequate remedy * * *" (*General Stores Corp. v. Shlensky*, 350 U.S. 462, 467), and this requires a "determin[ation] on the facts of the case whether the formulation of a plan under

their trailers for shares of Capitol Leasing stock, the president of Capitol and the officers and directors of the debtor were withdrawing their trailers from debtor and were leasing them to another concern engaged in a similar business, and were also urging their relatives to do the same. This was not disclosed to the trailer owners, nor were trailer owners furnished information of Capitol's financial condition or its management. Trailer owners were not told of pending proceedings involving other stock fraud charges against Capitol."

After hearing, a referee in bankruptcy denied the petition to intervene (Tr. 512-417). The district judge granted the petition to intervene but denied the relief sought (Tr. 596-597), and the court of appeals affirmed (R. 159-161). The Commission's appeal on the intervention issue was consolidated with the appeal from the denial of dismissal (R. 151). The court of appeals agreed that "if the stock involved here were not part of an arrangement, the disclosures made with regard to it would be clearly inadequate" and that there was no basis for holding that the investor-creditors here "are not entitled to as much information as are those persons acquiring stock under ordinary conditions" (R. 160). It concluded, however, that appropriate action could be taken by the district court (R. 160-161). We did not seek review of the court of appeals' ruling on this aspect of the case.

the control of the debtor, as provided by c. XI, or the formulation of a plan under the auspices of disinterested trustees, as assured by c. X and the other protective provisions of that chapter, would better serve 'the public and private interests concerned including those of the debtor' " (*id.* at 465).

A. In *Securities and Exchange Commission v. United States Realty Company*, 310 U.S. 434, this Court pointed out the numerous respects in which Chapter X of the Bankruptcy Act provides greater protection for public investors than Chapter XI. These include (except where liabilities are less than \$250,000) the "appointment of a disinterested trustee" to conduct "a thorough examination and study * * * of the debtor's financial problems and management" and "to send the report to all security holders"; and the formulation and sponsorship of a plan of reorganization by the trustee rather than by the management (*id.* at 449-450). "No comparable safeguards are found in Chapter XI. * * * Every phase of the procedure bearing on the administration of the estate and the development of the arrangement is under the control of the debtor. * * * There are no provisions for an independent study of the debtor's affairs by court or trustee, or for advice by them to creditors with respect to their rights or interests in advance of their consent to the arrangement." (*id.* at 450-451).

We submit that Chapter XI cannot be utilized to readjust the rights of public investor-creditors (as distinguished from readjusting the rights of creditors who are not investors and thereby indirectly affecting

public investors) and that any reorganization that directly changes their rights may be had only under Chapter X. For in such a situation their contract rights should not be altered without the important protections provided by Chapter X.

The facts of the present case dramatically illustrate why public investor-creditors need the protection of Chapter X. The debtor has never operated at a profit and its history and present precarious financial situation raise vital questions as to the best course for the future of the company, which can be answered only after a careful and disinterested study. Chapter XI makes no provision for such study and none has been made or is contemplated in this case. A study by a disinterested trustee is also needed to consider whether new management is required, and to investigate possible causes of action against the old management. The present plan fails to provide sufficient information to enable the public investors to make an informed judgment as to its merits, and a disinterested trustee is needed to advise them with respect to the merits and demerits of any proposed plan. Finally, the plan itself demonstrates that this debtor needs a more comprehensive reorganization than the mere arrangement of its unsecured debts which is permissible under Chapter XI. Here the debtor is not merely "arranging" its unsecured debts. The interest of the trailer owners is being changed from that of creditors of the debtor to stockholders of a successor corporation, and the debtor's business will be taken over by the latter. In any realistic sense, therefore, what is being done in

this case is not an "arrangement" of the debtor's unsecured debts but a "reorganization" of its business, and such a sweeping revamping of the company should be conducted under Chapter X.

B. Transfer to Chapter X was also required to insure that any plan of reorganization will provide "fair and equitable" treatment of the public investor-creditors. Chapter X provides that a plan may not be confirmed unless it is "fair and equitable." Although Chapter XI contained the same standard prior to 1952, it was deleted in that year.

The words "fair and equitable" in Chapter X are "words of art" having a well understood meaning in reorganizations * * * that in any plan of corporate reorganization unsecured creditors are entitled to priority over stockholders to the full extent of their debts and that any scaling down of the claims of creditors without some fair compensating advantage to them which is prior to the rights of stockholders is inadmissible." *Securities and Exchange Commission v. United States Realty Company*, 310 U.S. 434, 452. This Court has consistently required, in whatever context publicly-held corporations have been reorganized, that investor-creditors must be afforded full compensatory treatment before junior interests may participate. The present plan does not satisfy the "fair and equitable" standard, since the stockholders are being permitted to participate in the reorganized enterprise at the expense of the investor-creditors but without making any contribution to the company.

We submit that *General Stores* establishes that a transfer to Chapter X is mandatory whenever a pro-

posed plan of arrangement is not fair and equitable to public investor-creditors. For the Court there listed, as the first of a series of "typical instances where c. X affords a more adequate remedy than c. XI" (350 U.S. at 467), the following situation (*id.* at 466):

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Readjustment of all or a part of the debts of an insolvent company without sacrifice by the stockholders may violate the fundamental principle of a fair and equitable plan (see *Case v. Los Angeles Lumber Products Co.* * * *), as the *United States Realty Co.* case emphasizes.

The deletion of the "fair and equitable" requirement from Chapter XI by the 1952 amendments did not, contrary to the view of the court of appeals, sanction the use of that chapter to deprive public investor-creditors of the protection of that standard. The court of appeals' view is directly contrary to this Court's statement in *General Stores, supra*. Moreover, the legislative history of the 1952 amendments indicates that they were directed to a different problem—the use of Chapter XI for an arrangement of ordinary commercial debts—and were not intended to touch upon the problem of when a Chapter XI proceeding should be transferred to Chapter X.

C. The court of appeals improperly deferred to the discretion of the district court in affirming the order denying transfer. There was no problem here of delicately balancing conflicting considerations; where the trial court's evaluation and judgment might be accorded special weight. On the contrary, here all the pertinent factors compel transfer. The growing

tendency in the lower courts to regard Chapters X and XI as alternative remedies, the choice between which lies largely with the debtor, and to regard the district court's refusal to overturn the debtor's choice of the latter chapter as a matter within its discretion tends largely to nullify the reforms in reorganization law and practice which Chapter X sought to achieve. For the debtor and its trade creditors have strong reason to prefer the "speed and economy" of Chapter XI to the "thoroughness and disinterestedness" of Chapter X (*Realty*, 310 U.S. at 450-451). We therefore urge this Court to make it clear that a district court has no discretion to refuse a transfer where the rights of public investor-creditors are to be readjusted, or, at least, where the proposed arrangement would deny them "fair and equitable" treatment.

ARGUMENT

PROPER PROTECTION OF THE INTERESTS OF THE PUBLIC INVESTOR-CREDITORS OF A FINANCIALLY DISTRESSED CORPORATION REQUIRES THAT PROCEEDINGS FOR ITS REORGANIZATION BE CONDUCTED UNDER CHAPTER X OF THE BANKRUPTCY ACT RATHER THAN UNDER CHAPTER XI.

Section 328 of the Pankruptey Act (11 U.S.C. 728) in substance directs the district judge, upon the application of the Securities and Exchange Commission or any party in interest, to transfer a proceeding under Chapter XI of the Bankruptcy Act to Chapter X "if he finds that the proceedings should have been brought under" the latter chapter. Conversely, the district judge may not entertain a petition under Chapter X unless he is satisfied that "adequate re-

lief" would not be obtainable under Chapter XI (Sections 141, 146(2), 11 U.S.C. 541, 546(2)). The two chapters are thus mutually exclusive, and Chapter XI is not properly invoked "where c. X affords a more adequate remedy * * *" (*General Stores Corp. v. Shlensky*, 350 U.S. 462, 467). "[T]he adequacy of the relief under Chapter XI must be appraised in comparison with that to be had under Chapter X * * *" (*Securities and Exchange Commission v. United States Realty Co.*, 310 U.S. 434, 455), and this requires a "determin[ation] on the facts of the case whether the formulation of a plan under the control of the debtor, as provided by c. XI, or the formulation of a plan under the auspices of disinterested trustees, as assured by c. X and the other protective provisions of that chapter, would better serve 'the public and private interests concerned including those of the debtor'" (*General Stores, supra*, at 465). Since, as we shall show, Chapter X here "affords a more adequate remedy" than Chapter XI, "it was plainly the duty of the district court in the exercise of a sound discretion to have dismissed the [Chapter XI] petition, remitting respondent if it was so advised to the initiation of a proceeding under Chapter X, * * *". (*Realty*, 310 U.S. at 456-457).

Transfer of these proceedings to Chapter X was required for two reasons: *First*, it would be inappropriate to adjust the rights of public investor-creditors without giving them the benefit of the protective procedures which Congress provided in Chapter X for investors, generally. *Second*, since an arrangement under Chapter XI need not satisfy the "fair and equit-

able" standard which a plan of reorganization under Chapter X must meet, use of Chapter XI would permit a reduction in the rights of investor-creditors in order to give the junior security holders who control the management an interest in the reorganized company. In these circumstances, the decision whether to transfer did not turn upon any balancing of conflicting considerations which lay within the discretion of the district court. On the contrary, the undisputed facts of this case made a transfer mandatory.

A. THE PUBLIC INVESTOR-CREDITORS REQUIRE THE PROTECTION WHICH CONGRESS PROVIDED IN CHAPTER X FOR INVESTORS IN CORPORATIONS UNDERGOING REORGANIZATION.

1. INTRODUCTION

In *Securities and Exchange Commission v. United States Realty Co.*, 310 U.S. 434, the Court discussed the evils which led Congress to adopt the reorganization provisions of the Bankruptcy Act, and described in some detail the great protections which Chapter X provides for investors. Mr. Justice Stone, writing for the Court, pointed out (*id.* at 448) that among the conditions responsible for the enactment of Section 77B of the Bankruptcy Act, the predecessor to Chapter X, had been—

* * * the inadequate protection of widely scattered security holders, the frequent adoption of plans which favored management at the expense of other interests, and which afforded the corporation only temporary respite from financial collapse * * *

In order to protect public investors from overreaching by management in the formulation and im-

plementation of reorganization plans, Congress provided in Chapter X a comprehensive system of safeguards designed "to provide for a larger measure of control by the court over security holders' committees and the formulation of reorganization plans and to secure impartial and expert administrative assistance in corporate reorganizations through participation of the [Securities and Exchange] Commission," which is authorized "to participate generally in the proceedings as a party" with court approval and is required to do so if requested by the court. (*id.* at 449, 450). As the Court pointed out, "[a] large measure of control is given to the court over the reorganization * * *, §§ 163, 165, 209, 212, 241-243." Chapter X requires (except where liabilities are less than \$250,000) the "appointment of a disinterested trustee" who is to conduct "a thorough examination and study * * * of the debtor's financial problems and management" and "to send the report to all security holders." It is the trustee, and not the management, who formulates a plan of reorganization. Not until the judge approves the plan may it be submitted to creditors. § 176. It is then accompanied by "the report of the Commission and the opinion of the judge approving the plan, § 175."

"No comparable safeguards," the Court noted, "are found in Chapter XI" (*id.* at 450). It "provides a summary procedure by which a debtor may secure judicial confirmation of an 'arrangement' of his unsecured debts" (*id.* at 446). "Every phase of the procedure bearing on the administration of the estate

and the development of the arrangement is under the control of the debtor. The process of formulating an arrangement and the solicitation of consent of creditors, sacrifices to speed and economy every safeguard, in the interest of thoroughness and disinterestedness, provided in Chapter X. * * * The debtor proposes the arrangement * * * and the only opportunity afforded the creditors in respect to the proposed plan is to accept or reject it as submitted by the debtor. * * * There are no provisions for an independent study of the debtor's affairs by court or trustee, or for advice by them to creditors with respect to their rights or interests in advance of their consent to the arrangement. * * * "The court in passing upon the arrangement, is * * * faced with the fact that a majority of the creditors have already accepted the plan." *Id.* at 450-451. In short, any successful "arrangement" of the rights of creditors "if accomplished at all, must be without the aids to the protection of creditors and the public interest which are provided by Chapter X * * *" (*id.* at 453).

Because of the protection which Chapter X provided for security holders, this Court held in *Realty* that the district court should have dismissed the Chapter XI petition and left the debtor there to institute a proceeding under Chapter X, "in which it may secure a reorganization which, after study and investigation appropriate to its corporate business, structure and ownership, is found to be fair, equitable and feasible, and in the best interest of creditors" (*id.* at 457).

In *General Stores Corp. v. Shlersky*, 350 U.S. 462,

465, the Court upheld the lower courts' rulings that Chapter X rather than Chapter XI was required for the reorganization of the corporation there involved. It explained (p. 465) that in *Realty* it had emphasized that, in choosing between the two chapters, it was necessary to determine "whether the formulation of a plan under the control of the debtor, as provided by c. XI, or the formulation of a plan under the auspices of disinterested trustees, as assured by c. X and the other protective provisions of that chapter, would better serve 'the public and private interests concerned including those of the debtor.'" It stated (p. 466) that the "controlling consideration in a choice between c. X and c. XI" is "the needs to be served."

2. THE NEED FOR CHAPTER X PROCEDURES IN THE PRESENT CASE

We submit that these two decisions, read in the light of the basic purposes of the two chapters governing corporate readjustments (see *supra*, pp. 22-23), make it clear that Chapter XI cannot be utilized to readjust the rights of public investor-creditors (as distinguished from a readjustment of the rights of noninvestor-creditors which may indirectly affect investors); and that any reorganization that directly changes their rights may be had only under Chapter X. This is because in such a situation their contract rights should not be altered without the important protection provided by Chapter X—protection designed to give them the benefits of a thorough, impartial investigation of and report upon the conditions that led the debtor into difficulties, an objective eval-

uation of the competency of the management that was responsible therefor and an informed estimate whether new management is required, an independent study of possible causes of action against the management, and an objective analysis of the proposed plan, explaining both its virtues and its problems.

The facts of the present case dramatically illustrate why in such a situation "the formulation of a plan under the auspices of disinterested trustees *** and the other protective provisions" of Chapter X "would better serve 'the public and private interests concerned ***'" than its "formulation *** under the control of the debtor as provided by c. XI" (*General Stores, supra*) and without such protections for investors.

a. *The need for a disinterested trustee to make a thorough examination of the debtor's financial problems and management and to report thereon to the security holders.* The debtor has never operated at a profit. At an earlier period, its management apparently misappropriated substantial corporate funds. Most of the trailers were purchased from an affiliated company; a large number of them, although paid for, were either not manufactured or, if manufactured, were not delivered. The manufacturing company is bankrupt. Only two-thirds of the \$3,500,000 contributed by the public investors for the purchase of trailers was used for that purpose; the balance appears to have been drained off in high commissions taken by the management on the sale of the trailers' to the public. Portions of these commissions

on new trailer sales were, in turn, used by the management to pay prior purchasers of trailers the high rentals which they had been promised—running as much as 36 percent a year on their investment. When the debtor filed its petition for an arrangement, its stated liabilities of \$1,367,890 were approximately double its stated assets of \$685,608; most of the latter (\$500,000), however, represented the alleged value of the trailer rental system, i.e., the debtor's arrangements with the service station operators (see Statement, *supra*, p. 11).

In short, the debtor always has been in precarious financial condition, and apparently it was hopelessly insolvent, in both the bankruptcy and the equity sense, when the arrangement was sought. The debtor's disastrous financial history and unhappy operating experience immediately raise two vital questions: (1) why did it get into this predicament, and (2) what, if anything, can be done to remedy the situation, to put the company on a sound financial footing, and to prevent a recurrence of those disasters? Those basic questions in turn raise other fundamental problems —are the debtor's difficulties due to outside circumstances, general economic conditions in the industry, managerial incompetence or chicanery, or other factors? These obviously difficult questions require careful study, but unless and until they are answered it is impossible to write any meaningful prescription for the future economic health of the company.

Chapter XI, of course, makes no provision for such a study, and none has been made, or is intended to be made, in this case. But without such a study there

is no way of even attempting to predict, in a financial situation such as this, whether in the long run the company or creditors will really be any better off after the arrangement than it was before. True, the arrangement may temporarily solve the most pressing immediate financial problems—in this case, at the expense of the public investor-creditors and for the benefit of the stockholders, see *infra*, pp. 40-41—but such temporary relief may not even touch upon the real ills and needs of the enterprise.

Under Chapter X, as the Court explained in *Realty* (310 U.S. at 449-450), there would be "a thorough examination and study by the trustee of the debtor's financial problems and management." Section 167 (1), (2), (5), 11 U.S.C. 567(1), (2), (5). "The trustee is required to report the result of his study, to send the report to all security holders with notice to submit to him proposals for a plan of reorganization." Only by such a comprehensive analysis can the real causes of the debtor's difficulties be ascertained, and the proper methods for correcting them be established. Only Chapter X provides the procedure.

b. *The need for a disinterested trustee to recommend whether new management is required.* The district court recognized (R. 145)—as it necessarily had to do in the light of the facts in the record (see *supra*, pp. 7-11)—that "there may be in this situation need for new management, and there certainly is some question in my mind as to whether or not the management that is presently * * * operating it, would continue to do so for the best interests of the

investors." The court nevertheless did not find this to be a fact calling for transfer to Chapter X, since "that has not been clearly established yet" (R. 145); and it suggested (R. 145-146) that "if there is any indication of any criminal activity on the part of the people who are running the company, this should by the SEC be investigated and if found that there is any or has been any criminal activity should be reported to the proper authorities in the Justice Department."

But the whole purpose of transferring the proceeding to Chapter X is to give the independent trustee the opportunity to conduct a searching inquiry to determine whether new management is required. Such an inquiry plainly is required where the district court itself recognizes, as it did here, that "there may be * * * need for new management" and that there is doubt whether the existing management would continue to operate the company "for the best interests of the investors." The purpose of such an investigation is not to determine whether the management has violated the federal securities laws—although if it had, this plainly would bear upon its qualification to continue to hold its present positions of trust and confidence—but to ascertain whether the financial and operating changes necessary to solve the debtor's problems may not also require new people to make them effective. "Readjustment of the debts may be a minor problem compared with the need for new management. Without a new management today's readjustment may be a temporary moratorium before

a major collapse." *General Stores Corp. v. Shlensky*, 350 U.S. 462, 466.

c. *The need for a disinterested trustee to investigate possible causes of action against the management.* One of the innovations which Chapter X introduced into the reorganization process is the requirement that the trustee "report to the judge any facts ascertained by him pertaining to fraud, misconduct, mismanagement and irregularities, and to any causes of action available to the estate" (Section 167(3), 11 U.S.C. 567(3)). In the present case, such an investigation of and report on possible causes of action by the debtor against its past and present management plainly was necessary. For the debtor may have valid claims arising out of the substantial sums which apparently were misappropriated from it, the large additional amounts paid for trailers never manufactured or delivered to it, the granting to DeMar (which was affiliated with the debtor) of the exclusive contract to manufacture trailers, the delivery by DeMar of defective and unusable trailers, and the substantial portion of the amounts paid by public investors for trailers that was siphoned off through the high commissions charged on trailer sales (see *supra*, pp. 9-10). Investigation might also indicate the need to subordinate the debt claims which the management has against the debtor (R. 4, 6) to the claims of the public investor-creditors. Cf. *Taylor v. Standard Gas and Electric Co.*, 306 U.S. 307; *Mecca Temple v. Darrock*, 142 F. 2d 869 (C.A. 2),

certiorari denied, 323 U.S. 784; *In the Matter of Texas Portland Cement Co.*, 205 F. Supp. 159 (E.D. Tex.), note 13, *infra*.

There is no method by which such an investigation can be made under Chapter XI, and none either has been made or is contemplated. For, as Mr. Justice Douglas stated in testifying as Chairman of the Securities and Exchange Commission on the proposed corporate reorganization provisions in 1937, "a debtor in possession cannot be expected to investigate itself" (Hearings on H.R. 6439 before the House Committee on the Judiciary, 75th Cong., 1st Sess., 175-176). Only an independent trustee appointed under Chapter X can and would make such a study. While it cannot be predicted whether an investigation in this case would ultimately produce any tangible benefits for the debtor,¹³ there is certainly enough in this record

¹³ There have been a number of recent cases in which comprehensive investigations by Chapter X trustees have resulted in substantial benefits and recoveries on behalf of the debtors' estates. See *Twenty-Eighth Annual Report of the Securities and Exchange Commission* (Government Printing Office: (1963) 98. For example, in *In the Matter of Texas Portland Cement Co.* (E.D. Tex., No. 1606), such investigation led to a reduction in the debtor's total indebtedness from approximately \$5,200,000 to about \$3,150,000 and the cancellation or surrender of almost 215,000 shares of capital stock. The confirmed plan of reorganization also provided for the subordination to public securityholders of certain claims of the debtor's directors who had not settled with the trustee, 205 F. Supp. 159, 162 (E.D. Tex., 1962). In *In the Matter of Shawano Development Corporation* (D. Wyo. No. 3163), the trustee has instituted actions against twenty-two defendants on the basis of the investigation conducted, and approximately \$3,000,000 is claimed. *In the Matter of DePaul Educational Aid Society*, (N.D. Ill., No. 59 B 41), involved a claim which

to warrant a comprehensive inquiry. "Readjustment of the debt structure of a company, without more, may be inadequate unless there is also an accounting by the management for misdeeds which caused the debacle". (*General Stores, supra*, 350 U.S. at 466).

d. *The need for a disinterested trustee to formulate the plan of reorganization and to advise the security-holders thereon.* Under Chapter XI, the debtor itself formulates the plan of adjustment, and it is no surprise that the plan which the debtor here proposes requires the public investors to accept a significant reduction in their interest in the company. The plan, however, fails to provide sufficient information to enable the public investors to make an informed judgment as to its merits, but instead gives them no practical alternative but to accept it; makes no attempt to explain why such sacrifice is required; and offers

was discovered upon investigation and was settled by a creditor agreeing to reduce its claim by 45 percent.

In *In the Matter of Automatic Washer Company* (S.D. Iowa, No. 5-426), the trustee after investigation obtained a judgment for the debtor of \$406,250 and also recovered some \$90,000 in settlement of claims, including one for fraud in the alleged sale of machinery to the debtor. In *In the Matter of Swan-Finch Oil Corp.* (S.D. N.Y., No. 93046), the trustees have instituted various actions including a suit for \$6 million and have effected very substantial recoveries on behalf of their estates as a result of their investigations. *Twenty-Ninth Annual Report of the Securities and Exchange Commission* (Government Printing Office: 1964) 90-91. See also *Pettit and Crawford, Trustees v. Doeskin Products, Inc.*, 270 F. 2d 95 (C.A. 2), rehearing denied, *id.* at 599, and *Pettit and Crawford, Trustees v. Olean Industries*, 266 F. 2d 833 (C.A. 2).

no appraisal of the likelihood of successful operation if it is adopted.

The typical investor-creditor of the debtor has (1) a trailer, which, if it can be found, will be located at a gasoline service station probably hundreds of miles from his residence, (2) a contractual right to receive a fixed rent from the debtor for his trailer, and (3) a substantial claim against the debtor for past rent. Investors who have paid for but have not received their trailers have a claim for the purchase price. The proposed arrangement requires the investor-creditors to surrender their trailers, their right to future rent and their claims for unpaid rent or for their purchase price, and to take in return stock in a corporation newly organized by persons affiliated with the debtor. The amount of stock the investor-creditors are to receive is to be determined not by the actual value of the trailers they are asked to sell nor by the value of their claims to past or future rent. Instead, investor-creditors are to receive one share of stock of the new corporation for every \$2.00 of their "remaining capital investment," calculated on the basis that any rent which a trailer owner may have received was actually a return of capital rather than income, as he presumably assumed when he made his investment.

The plan of arrangement is silent with respect to a number of important things which the investor-creditors should know if they are to make an informed judgment on whether to accept or reject it. For example, the plan does not state the consequences if an investor rejects it. Presumably he is free to take pos-

session of his trailer, if he can find it; the plan does not indicate what effort, if any, the debtor or its successor will make to aid him in doing so. Nor does it state whether a non-accepting investor's claim for back rentals is wiped out, or whether it may be asserted against Capitol, the successor corporation.

The plan is written so as to confuse rather than help an unsophisticated investor. For after first stating that "Unsecured debts shall be paid and satisfied as follows," it then goes on to provide that the \$710,597.53 due the trailer-owners shall be "satisfied" by the issuance to them of Capitol stock, upon receipt of certificates of title to the trailers, on the basis of one share for each \$2 remaining capital investment in the trailers (R. 6). An unsophisticated investor reading this description of the plan might not realize that the stock he is to receive is in exchange for his remaining investment in the trailer, and that his claim for unpaid rent is being "paid and satisfied" by his giving it up.

The plan contains no estimate of future earnings of the reorganized company, no indication of how the management intends to change the operation which thus far has been unsuccessful, and no reasons why the management believes that the proposed changes are likely to produce a successful venture. All that the plan contains with respect to those vital matters is the brief statement (R. 7-8):

The proponents of this plan believe that it is feasible—and submit that the adoption of the plan by trailer owners and creditors will allow

Capitol Leasing Corporation and the debtor the opportunity to combine their resources with the result that the business operation may be carried on successfully. Unless the plan is adopted, proponents suggest that creditors will receive little, if anything, in settlement of debtor's obligation to them, and that trailer owners may find themselves unable to realize any value for their trailers or any income from their operation.

This threat of disaster unless the investor-creditors accept the plan, coupled with the lack of the detailed facts which they need to make an intelligent judgment, makes a mockery of the choice which the plan purports to offer. An investor-creditor can either attempt to obtain possession of his trailers (which presumably he never wanted) or give up the trailers and claims against the debtor for stock in a corporation about which he is given virtually no information. Should any investor-creditors adopt the first alternative, they are warned they may not be able to "realize any value for their trailers" and they are left unclear whether their past claims are wiped out. Should they adopt the second, they would receive an interest in a corporation about which they know almost nothing except that there is cause for concern about the management's competency or good faith.

The short of the matter is that here, just as in *Securities and Exchange Commission v. Liberty Baking Corp.*, 240 F. 2d 511, 515 (C.A. 2), certiorari denied, 353 U.S. 930, the investors affected "cannot competently appraise [the] proposed plan without the educated advice of [a]. * * * disinterested person."

Cf. *Mecca Temple v. Darrock*, 142 F. 2d 869, 871 (C.A. 2); certiorari denied, 323 U.S. 784, where the court assumed that many of the public investors "do not even know of the pendency of these proceedings, and that many who have been informed suffer from a grave lack of accurate information as to the true state of affairs." In each of those cases the Second Circuit, in reversing a district court's refusal to transfer a Chapter XI proceeding to Chapter X, gave significant weight to the fact that under Chapter XI the public investors would not be given the necessary information which a Chapter X trustee would furnish. The same consideration is equally persuasive in favor of transfer here.

Finally, in view of the Commission's charge that the management made false and misleading statements in soliciting acceptances of the plan (see note 12, *supra*, pp. 14-15), and the court of appeals' recognition (R. 160) that "if the stock involved here were not part of an arrangement, the disclosures made with regard to it would be clearly inadequate," there is reason to question whether any additional information which the present management might furnish to the public investor-creditors would provide a full and objective analysis of the plan, including its deficiencies as well as its virtues.

e. *The need for a more comprehensive reorganization than a mere arrangement of unsecured debts under Chapter XI.* The proposed plan on its face involves more than a mere "arrangement" of the company's unsecured debts. In a typical Chapter XI ar-

angement, unsecured creditors may extend the maturity of their indebtedness, change its terms or reduce its principal amount, or agree to any combination of these things. After the arrangement, however, they still remain unsecured creditors, and the debtor continues in its same corporate form.

Under the present plan, however, the company is doing something quite different from simply "arranging" its unsecured debts. It is turning its business over to another corporation, and it is eliminating those debts by converting its creditors into stockholders in the new company. In connection with such conversion, the creditors are turning their own property and claims over to the new corporation in exchange for the latter's stock. If the arrangement is consummated, the public investor-creditors will have ceased to exist as such, and the debtor presumably will be liquidated, since its business will be conducted by its successor. There would thus be a complete change in both the form and the financial structure of the business.

Moreover, the claims of trailer owners are not ordinary unsecured debts of the company. These creditors acquired title to their trailers in order to secure payment of the amounts to be paid to them, creating what in economic substance is a secured claim.¹⁴ Un-

¹⁴ The accounting treatment of such claims is of interest. It is not clear whether or not the amounts to become due to trailer owners would have to be shown on the debtor's balance sheet as a liability. See Accounting Research Bulletin No. 38 (American Institute of Accountants, 1949), dealing with sale and lease-back arrangements. If such amounts were required to appear as a liability, which is quite possible, then

der the plan they are to relinquish this secured interest. The desire of the debtor to eliminate that interest is presumably one reason for the proposed structural changes in the business. Chapter XI, of course, is available to readjust only "the rights of unsecured creditors of the debtor * * *," (*Realty*, 310 U.S. at 452; Section 306(1), 11 U.S.C. 706(1)).

What is involved in this case, therefore, in any realistic sense is not an "arrangement" of the debtor's unsecured debts but a "reorganization" of its business. Even if this far-reaching revamping of the debtor's capital structure and form could come within the statutory definition of "arrangement" in Chapter XI,¹⁵ we submit that a corporate reorganization which goes beyond a simple "adjustment" of unsecured debts should be conducted as a reorganization under Chapter X and not as an adjustment under Chapter XI. Cf. *Securities and Exchange Commission v. United States Realty Co.*, 310 U.S. 434, 447, 456. Here the breadth of the plan which management itself has proposed fully confirms what is obvious from the history and present financial predicament of the debtor, namely, that "this business needed a more pervasive reorganization than is available under c. XI" (*General Stores, supra*, 350 U.S. at 468).

they should be shown as secured by the trailers. See Securities and Exchange Commission Regulation SX, Rule 5-02(30), 17 CFR 210.5-02(30).

¹⁵ Section 306(1) of the Bankruptcy Act (11 U.S.C. 706(1)) defines "arrangement" for the purposes of Chapter XI as—

* * * any plan of a debtor for the settlement, satisfaction, or extension of the time of payment of his unsecured debts, upon any terms.

B. THE USE OF CHAPTER X IS REQUIRED TO INSURE THAT ANY PLAN OF REORGANIZATION IS "FAIR AND EQUITABLE" TO THE PUBLIC INVESTOR-CREDITORS.

Chapter X requires that, before the judge may confirm a plan of reorganization, he must be satisfied that "the plan is fair and equitable, and feasible" (Section 221(2), 11 U.S.C. 621(2)). Prior to 1952, Chapter XI contained the same standard. In that year, however, it was amended to delete the requirement that the plan be "fair and equitable" (66 Stat. 433), and it now requires only that the plan be, among other things, "feasible" (Section 366(2), 11 U.S.C. 766(2)).

The words "fair and equitable" in Chapter X are "words of art" having a well understood meaning in reorganizations * * * that in any plan of corporate reorganization unsecured creditors are entitled to priority over stockholders to the full extent of their debts and that any scaling down of the claims of creditors without some fair compensating advantage to them which is prior to the rights of stockholders is inadmissible." *Securities and Exchange Commission v. United States Realty Co.*, 310 U.S. 434, 452. This Court has consistently required, in whatever context publicly-held corporations have been reorganized, that investor-creditors must be afforded full compensatory treatment before junior interests may participate. See e.g., *Northern Pacific Railway v. Boyd*, 228 U.S. 482, 502, 504 (equity receivership); *Casé v. Los Angeles Lumber Co.*, 308 U.S. 106, 115-116 (reorganization under Section 77B of the Bankruptcy Act); *Consolidated Rock Products Co. v. DuBois*, 312 U.S. 510, 527-529 (reorganization under Section 77B of the

Bankruptcy Act); *Ecker v. Western Pacific R. Corp.*, 318 U.S. 448, 484 (railroad reorganization under Section 77 of the Bankruptcy Act); *Otis & Co. v. Securities and Exchange Commission*, 323 U.S. 624, 633-640 (reorganization under the Public Utility Holding Company Act of 1935). As explained in *Consolidated Rock Products*, 312 U.S. at 527, 529:

"any arrangement of the parties by which the subordinate rights and interests of the stockholders are attempted to be secured at the expense of the prior rights" of creditors "comes within judicial denunciation." *Louisville Trust Co. v. Louisville, N. A. & C. Ry. Co.*, 174 U.S. 674, 684. * * *

If [creditors] receive less than * * * full compensatory treatment, some of their property rights will be appropriated for the benefit of stockholders without compensation. That is not permissible. * * *

The present plan does not satisfy the "fair and equitable" standard. Since the debtor is insolvent, the entire enterprise, whatever its value, belongs to the creditors; and the stockholders cannot participate unless they contribute some additional money or property to the reorganized enterprise. The stockholders here are not making any such contribution; the suggestion in the plan that they are, because the debtor will transfer its rental system to the new corporation (R. 5), ignores the fact that since the debtor is insolvent its system belongs to the creditors, not to the stockholders. The plan proposes the distribution to the stockholders of the 107,100 shares of Capitol stock to

be issued to the debtor in exchange for its trailer-rental system; to that extent the "property rights [of the public investor-creditors] will be appropriated for the benefit of stockholders without compensation" (*Consolidated Rock Products, supra*): There is thus present in this case that "scaling down of the claims of creditors without some fair compensating advantage to them which is prior to the rights of stockholders" which, according to *Realty*, "is inadmissible." The extent of the inadmissible scaling down of the investor-creditors' rights is reflected in the fact that they are to receive no compensation for the \$700,000 back rent owing to them, and that the rent already received is to be treated retroactively as a return on capital.

Thus, if the present arrangement were part of a plan of reorganization under Chapter X, it could not be approved as "fair and equitable." The question is whether that standard, designed to protect creditors of a financially-distressed corporation from having their claims diminished for the benefit of junior interests, may be avoided by proceeding under Chapter XI.

We submit that *General Stores* establishes that a transfer to Chapter X is mandatory whenever a proposed plan of arrangement is not fair and equitable to public investor-creditors. For the Court there listed, as the first of a series of "typical instances where c. X affords a more adequate remedy than c. XI" (350 U.S. at 467), the following situation (*id.* at 466):

Readjustment of all or a part of the debts of an insolvent company without sacrifice by the

stockholders may violate the fundamental principle of a fair and equitable plan (see *Case v. Los Angeles Lumber Products Co.*, * * *), as the *United States Realty Co.* case emphasizes.

In *Realty* transfer to Chapter X was required because, even though Chapter XI then contained the "fair and equitable" standard, its procedures were not adequate to insure that the standard would be met (310 U.S. at 453-454). The present case seems *a fortiori*, since here "fair and equitable" treatment would be provided only under Chapter X.¹⁸

Thus, Chapter XI may not be utilized where the plan requires the investor-creditors to give up part of their claims without some compensating "sacrifice by the stockholders." To permit Chapter XI to be utilized in that situation would run counter to the numerous decisions of this Court refusing to permit a corporate reorganization in which senior interests did not receive "fair and equitable" treatment. See the cases cited *supra*, pp. 39-40. It would also ignore the fact that one of the evils which gave rise to the reorganization provisions of the Bankruptcy Act was,

¹⁸ Our argument assumes—and we do not understand the respondent to dispute it—that the proposed plan of arrangement in the present case does not meet the fair and equitable standard. See *supra*, pp. 40-41. But even if that issue were less clear than we believe it to be, that would not justify the denial of transfer. For, as *Realty* makes clear (310 U.S. at 454), the determination whether the present plan is fair and equitable "obviously cannot be answered with any assurance in the present case without resort to the facilities for investigation of the financial condition and structure of the debtor * * * and to the expert aid and advice of the Commission available under Chapter X."

"the frequent adoption of plans which favored management at the expense of other interests" (*Realty*, 310 U.S. at 448).

The court of appeals, however, concluded that the 1952 amendments of Chapter XI sanction the use of that chapter for an arrangement which does not provide fair and equitable treatment of investor-creditors (R. 157-159). It relied on provisions of those amendments which (a) deleted from Chapter XI the requirement that the plan be fair and equitable, and (b) added a provision stating that confirmation of an arrangement "shall not be refused solely because *** the interests of [a corporate debtor's] stockholders or members will be preserved" (Section 366, 11 U.S.C. 766).

The court of appeals' conclusion is directly contrary to this Court's statement in *General Stores*, *supra*, pp. 41-42, that the failure of a plan of arrangement under Chapter XI to satisfy the fair and equitable standard would call for the use of Chapter X. The *General Stores* decision was rendered in 1956, four years after the 1952 amendments. That this Court was fully aware of those amendments when it made the statement in *General Stores* is shown by the reliance upon those amendments in the dissenting opinion, 350 U.S. at 471-472.

In other words, the fact that a plan of arrangement under Chapter XI need no longer satisfy the "fair and equitable" standard may be the very reason why that chapter does not provide adequate relief where the interests of public creditors are being ad-

versely affected for the benefit of junior security holders. Thus, in *Securities and Exchange Commission v. Liberty Baking Corporation*, 240 F. 2d 511, 515 (C.A. 2), certiorari denied, 353 U.S. 930, the court stated that because there was "a grave question whether the plan would deprive creditors of their 'absolute priority' rights as against stockholders, * * * the need for resort to Chapter X is much greater than was the need in General Stores."

Moreover, the legislative history of the 1952 amendments indicates that they were directed to a different problem—the use of Chapter XI for an arrangement of ordinary commercial debts—and were not intended to touch upon the problem of when a Chapter XI proceeding should be transferred to Chapter X. The deletion of the "fair and equitable" standard from Chapter XI was viewed as a mere "clarifying" and "uncontroversial" amendment.¹⁷ It would hardly have been so described if it had been intended to effect substantive changes in the law governing

¹⁷ H. Rep. No. 2320, 82d Cong., 2d Sess., pp. 2-3. See also S. Rep. No. 1395, 82d Cong., 2d Sess., p. 20, where, in a letter to the Chairman of the Senate Judiciary Committee, the Assistant Director of the Administrative Office of the United States Courts stated, with respect to the Senate bill embodying the 1952 amendments, that it was "designed to correct certain inaccuracies, ambiguities, and minor imperfections in the National Bankruptcy Act that have been revealed since the enactment of the Chandler Act in 1938. Nearly all of the proposals are regarded as noncontroversial in character." A chart prepared by the National Bankruptcy Conference, which initiated these amendments, classified Section 35 of the bill, deleting the "fair and equitable" language, as a "perfecting or clarifying" amendment. *Id.*, at 23.

the transfer of Chapter XI proceedings to Chapter X.¹⁸

A more probable explanation of the amendment is that Congress was merely recognizing the fact, to which the *Realty* case had referred, that a conventional composition with trade creditors under Chapter XI could hardly involve the absolute priority doctrine, since by definition such a composition modifies the claims of these creditors without alteration of the rights of stockholders.¹⁹ This explanation of the 1952

¹⁸ This conclusion is supported by the fact that the same legislation added Section 328 to Chapter XI, which specifically authorizes the Securities and Exchange Commission or any party in interest to apply for the dismissal of a Chapter XI proceeding unless it should in effect be transferred to Chapter X. The House Committee Report states that this section "codifies the law of the United States Realty & Improvement case" (H. Rep. No. 2320, 82d Cong., 2d Sess., p. 19). This apparently refers to the procedure sanctioned in that case of moving to dismiss the Chapter XI proceeding. The Report, however, in the previous paragraph had referred to the substantive holding of *Realty*, and, if the legislation had been intended to alter that holding, the Report would certainly have criticized it.

¹⁹ Cf. *Realty*, 310 U.S. at 454:

While this means that arrangements of unsecured debts of corporations, like respondent, may not be "in the best interests of creditors" and "feasible" under Chapter XI, it does not mean that there is no scope for application of that chapter in many cases where the debtor's financial business and corporate structure differ from respondent's. This is especially the case with small individual or corporate business where there are no public or private interests involved requiring protection by the procedure and remedies afforded by Chapter X. In cases where subordinate creditors or the stockholders are the

legislation realistically reflects the different economic positions of public investor-creditors and ordinary commercial creditors, and explains why Congress was willing to permit the claims of the latter, but not of the former, to be cut down in a Chapter XI arrangement.

For it is one thing if informed business men, in order to retain a customer which is seeking to extricate itself from financial difficulties, are willing to accept a reduction of their claims without any change in the junior security interests. It is quite another, however, if public investor-creditors are required to accept less than their full claims in a reorganization because junior interests propose a plan under which they themselves participate. Commercial creditors, moreover, normally extend credit for short periods on the expectation that cash generated from current operations will be adequate to assure payment; their credit risks reflect basically an appraisal of short-term prospects, as indicated by the debtor's current assets and liabilities. Public investor-creditors, on the other hand, are seldom close to the management or operations of the debtor; they expect to recover their investment at the end of a stated period and the quality of their investment is dependent not only on the debt-

managers of its business, the preservation of going-concern value through their continued management of the business may compensate for reduction of the claims of the prior creditors without alteration of the management's interests, which would otherwise be required by the *Boyd* case. See *Case v. Los Angeles Lumber Products Co., supra*, [308 U.S. at pages] 121, 122.

or's ability currently to meet its obligations but also on the over-all asset coverage for their claims, represented by the equity capital contributed by the stockholders. A composition of the public investor-creditors' claims diverts to the stockholders, for whose benefit the loan was made, the very values upon which these creditors depended in making the loan, and without affording them an opportunity for recoupment.

In these circumstances, the court below erred in thinking that support for its decision below could be drawn from the statement in the House Committee Report on the 1952 amendments that those changes were (R. 158) "designed to remove the fair and equitable provision, and * * * made clear that the rule of the Boyd and Los Angeles cases shall not be operative under those three chapters [Chapters XI, XII, XIII]" (H. Rep. No. 2320, 82d Cong., 2d Sess., p. 21). For, as we have indicated, the apparent reason for the deletion of the "fair and equitable" standard from Chapter XI was not to change the principles governing transfer to Chapter X, but to make it clear that an ordinary composition with trade creditors could be effected under Chapter XI. This conclusion is supported by the following statement in the House Committee Report, which precedes the language quoted by the court of appeals:

In fact, however, the fair and equitable rule * * * cannot realistically be applied in a chapter XI, XII, or XIII proceeding. Were it so applied, no individual debtor and, under chapter XI, no corporate debtor where the stock ownership is substantially identical with management could effectuate an arrangement except by payment of the claims of all creditors in full.

Chapter XI has replaced the old composition procedure under former section 12 of the Bankruptcy Act, where the fair and equitable rule did not apply. Nor is it practicable or realistic to apply the rule in a proceeding under chapter XI, XII, or XIII.²⁰

In other words, removal of "the fair and equitable" requirement from Chapter XII, dealing with real property arrangements and explicitly inapplicable to corporations (Section 406(6), 11 U.S.C. 806(6)), from Chapter XIII, dealing with wage earners' plans and applicable only to individuals (Section 606(8), 11 U.S.C. 1006(8)), and from Chapter XI, which, unlike Chapter X, may have individuals as well as corporations as the subject of proceedings, was intended to make arrangements possible for individuals or for privately-held corporate debtors. It was not intended to permit the rights of investor-creditors to be readjusted.

Moreover, our view is also consistent with the legislative history of Chapter XI showing that it was designed primarily to enable small businesses to effect compositions with trade creditors.²¹ Cf. *Realty*, 310

²⁰ H. Rep. No. 2320, 82d Cong., 2d Sess., p. 21. See also S. Rep. No. 1395, 82d Cong., 2d Sess., pp. 11-12.

²¹ This Court pointed out in *Realty*, 310 U.S. at 450, fn. 8, that "Chapter XI was sponsored by the National Association of Credit Men and other groups of creditors' representatives expert in bankruptcy." *Id.* at 450, fn. 8. See Hearings on H.R. 6439 before the House Committee on the Judiciary, 75th Cong., 1st Sess., p. 47, where one of the draftsmen of Chapter XI testified that its provisions were designed for the debtor who was "interested in making a composition with his mer-

U.S. at 447, where the Court pointed out that Chapter XI was "specifically devised to afford * * * procedures * * * adapted * * * to composition of debts of small individual business[es] and corporations with few stockholders * * *."

In short, the deletion of the "fair and equitable" standard from Chapter XI "had nothing whatsoever to do with the question of which procedure was to be required in a particular case; it dealt only with the [standards for] confirmation of an arrangement after that procedure had been decided upon and substantially completed," i.e., in cases where Chapter XI was properly invoked. *Grayson-Robinson Stores, Inc. v. Securities and Exchange Commission*, 320 F. 2d 940, 952 (C.A. 2) (dissenting opinion of Judge Clark on petition for rehearing *en banc*).

C. THE DENIAL OF TRANSFER CANNOT BE UPHELD AS A VALID EXERCISE OF THE DISTRICT COURT'S DISCRETION.

1. In affirming the district court's denial of transfer, the court of appeals relied primarily on its view that the matter lay within the discretion of the trial court. For the appellate court stated (R. 159): "[S]ince the granting of the motion rests in the dis-

chandise creditors." And see the statement of a representative of the National Bankruptcy Conference at the hearings, *id.* at 45:

Subsection I [Chapter XI] is no different from the present section 12 which has been with us for year[s], except that it allows wider rights. A man goes in, who has a little business as a druggist, and wants to make a composition with his creditors.

The cases for which Chapter XI was intended were also referred to in the hearings as "hot-dog stand" cases (*id.* at 175).

cretion of the court, while we think this is a borderline case, it does not appear that the S.E.C. has shown that adequate relief is not obtainable in Chapter XI proceedings or that there has been an abuse of that discretion warranting reversal."

Such deferral to the discretion of the district court was unwarranted. There was no problem here of delicately balancing conflicting considerations, where the trial court's evaluation and judgment should be accorded special weight. On the contrary, as we have shown, here all the pertinent considerations require transfer. The record can be searched in vain for any factors that support utilization of Chapter XI here, let alone outweigh the factors that call for transfer to Chapter X.

Nor can this Court's decision in *General Stores* fairly be read as indicating that the decision whether to transfer in this case was a matter within the discretion of the lower courts. In that case the district court had ordered transfer, and the court of appeals had affirmed. This Court, after pointing out (350 U.S. at 468) that it "was the view of two lower courts" that the debtor there "may well need a more thoroughgoing capital readjustment than is possible under c. XI," stated (*ibid.*): "We could reverse them only if their exercise of discretion transcended the allowable bounds. We cannot say that it does. Rather, we think that the lower courts took a fair reading of c. X and the functions it serves and reasonably concluded that this business needed a more pervasive reorganization than is available under c. XI."

The Court's broad statement of deferral to the discretion of the lower courts must be read in the light of the case before the Court. For the Court made that statement only after it had summarized the numerous factors which indicated that "the needs to be served" required use of Chapter X (*id.* at 467-468), and it immediately followed it with limiting language indicating that the lower courts had "reasonably concluded" that the public interest there required Chapter X. In other words, the Court was merely ruling that, on the record before it, both courts had correctly concluded that transfer was required. There is certainly no implication in *General Stores* that if both lower courts there had refused to transfer, this Court would have deferred to such action as a valid exercise of discretion. Indeed, the *Realty* case itself, where the district court refused to transfer and the court of appeals dismissed the appeal, makes it clear that if such refusal is improper, this Court will correct the error.

In this case, unlike *General Stores*, the decisions of the lower courts have "transcended the allowable bounds." Here, as was the situation in *Realty* (310 U.S. at 456-457), "it was plainly the duty of the district court in the exercise of a sound discretion to have dismissed the petition; remitting respondent if it was so advised to the initiation of a proceeding under Chapter X, in which it may secure a reorganization which, after study and investigation appropriate to its corporate business structure and ownership, is found to be fair, equitable and feasible, and in the best interest of creditors."

2. The court of appeals' view that the decision whether to transfer is a matter for the discretion of the district court reflects an apparently growing tendency in the lower courts to regard Chapters X and XI as alternative remedies, the choice between which lies largely with the debtor. Cf. *Grayson-Robinson Stores, Inc. v. Securities and Exchange Commission*, 320 F. 2d 940, 948 (C.A. 2), where the court stated that "Congress has authorized a corporate debtor seeking rehabilitation to follow either of two roads * * *." Since this view is usually coupled with the assumption of broad discretion in the district court to determine whether Chapter XI has been properly invoked, the tendency of this approach is to nullify in large part the reforms in reorganization law and practice which Chapter X sought to achieve.²²

For the debtor and its trade creditors will almost invariably prefer the "speed and economy" of Chapter XI to the "thoroughness and disinterestedness" of Chapter X (*Realty*, 310 U.S. at 450-451). To the management, a proceeding in which it remains in control and determines the future form of the business is obviously preferable to one in which it is supplanted by a disinterested trustee one of whose tasks is to investigate the conduct of the management. Similarly, trade creditors are likely to prefer the certainty of continued business relationships with

²² See Rostow and Cutler, *Competing Systems of Corporate Reorganization: Chapter X and XI of the Bankruptcy Act*; 48 Yale L. J. (1939) 1334; Jennings, *Mr. Justice Douglas: His Influence on Corporate and Securities Regulation*, 73 Yale L. J. (1964) 920, 935-941, 952-962.

existing management over the uncertainty of future business opportunities first under an independent trustee and then with a new management. Furthermore, when the district court considers a motion to transfer in such circumstances, it will normally be reluctant to override the deliberate choice of the parties to proceed under Chapter XI. This is particularly so since the scattered public investors are unlikely to be represented at the early stage of the proceedings; and the Commission, with its limited manpower and short time for investigation, ordinarily will be unable to develop all the pertinent facts which, were they known, might be sufficient to persuade the district court to reject the self-serving testimony of the other parties and to order transfer.²³ If, on the other hand, the decision whether to transfer is to be postponed until there has been a more thorough inquiry, the steps which have been taken in the interval in moving forward with the plan of arrangement will make the parties more likely to oppose transfer, and the court more reluctant to direct it.

²³ For example, in *In re Lea Fabrics, Inc.*, 272 F. 2d 769, 772 (C.A. 3), vacated as moot, 363 U. S. 417 (1960), the court of appeals affirmed denial of a motion to dismiss a Chapter XI proceeding and characterized allegations of this Commission as to management improprieties as "vague suspicions." On the ensuing bankruptcy of the same debtor, the district court referred, among other things, to "[management's] conceded looting of Lea's assets," noted that "[management] was 'bleeding' Lea with the knowledge and cooperation of [certain creditors]" and stated "The equities of the bankrupt's innocent creditors must prevail over the claims of the manipulator *** and his collaborating loan-participants ***." *In re Lea Fabrics, Inc.*, 226 F. Supp. 232 at 239, 240, 241 (D. N. J. 1964).

In short, leaving it largely to the discretion of the district court to decide whether to transfer cases would result in denying public security holders the protections which Congress intended them to have when it set up the different methods of reorganization provided by Chapters X and XI. For these reasons, we urge this Court to make it clear that a district court has no discretion to refuse a transfer where the rights of public investor-creditors are to be readjusted or, at least, where the proposed plan of adjustment denies them "fair and equitable" treatment.²⁴

²⁴ We do not go so far as to urge that Chapter XI can never be used where a company has publicly-held debt. There might be a case where a composition with merchandise creditors would be sufficient to solve a company's temporary financial problems, and there would be no need to alter the rights of its investor-creditors. See, e.g., *Securities and Exchange Commission v. Wilcox-Gay Corp.*, 231 F. 2d 859, 860 (C.A. 6), where, although there were publicly-held debentures, the arrangement approved scaled down only the claims of "general [trade] creditors."

CONCLUSION

The judgment of the court of appeals should be reversed, and the cause remanded with instructions to dismiss the Chapter XI proceedings.

Respectfully submitted.

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AUGUST, 1964.

APPENDIX

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Table Showing Comparisons of Sections in
Chapters X and XI of the Bankruptcy Act

	Chapter X	Chapter XI
1. Initiation of proceeding.	Debtor, three creditors, or indenture trustee may file petition (Sec. 120). Trustee appointed in every case in which indebtedness is \$250,000 or more (Sec. 156).	Only debtor may file petition (Sects. 321, 322). <i>No comparable provision.</i>
2. Appointment of trustee.		If trustee in bankruptcy has already been appointed, he must be continued in possession. Otherwise, receiver may be appointed "if necessary" (Secs. 332, 343). <i>No comparable provision.</i>
3. Qualifications of trustee.	Must be independent, disinterested (Sects. 156, 158).	Court may direct examination by creditor or other party of witnesses concerning acts, conduct, or property of debtor (Sec. 21a). <i>No comparable provision.</i>
4. Examination of Debtor's financial problems and causes of failure.	Trustee investigates property, liabilities, and financial condition of debtor, the operation of the business, and the desirability of its continuance (Sec. 167 (3); cf. Sec. 167 (1)). See also Sec. 21 (a).	
5. Report to Judge upon past conduct of the Debtor.	Trustee reports to judge facts pertaining to fraud, misconduct, mismanagement and irregularities, and any causes of action available to estate (Sec. 167 (3)).	
6. Reports to security holders.	Trustee submits statement of his investigation to security holders (Sec. 167 (3)).	<i>No comparable provision.</i>
7. Formulation of plan.	Trustee gives notice to security holders that they may submit to him suggestions for formulation of plan (Sec. 167 (6)).	<i>No comparable provision.</i>
8. Proposal and filing of plan.	Trustee prepares and files plan (or report of reasons why plan cannot be effected) before debtor may propose plans or amendments (Sec. 169).	<i>Only debtor may propose arrangement (Sec. 323) or modifications (Sec. 363).</i>
9. Assistance of administrative agency.	In cases in which the scheduled indebtedness exceeds \$3,000,000, and in other cases if the judge desires, plans which the judge finds worthy of consideration, after hearing, are submitted to the Securities and Exchange Commission for examination and report (Sects. 172, 173). Commission may, with approval of judge, participate in proceeding as a party (Sec. 208).	<i>No comparable provisions.</i>
10. Fairness of plan.	Plan may be approved and confirmed only if "fair and equitable, and feasible" (Sects. 174 and 221 (2)).	Plan may be confirmed if in "best interests of the creditors and is feasible" (Sec. 366). <i>No comparable provision.</i>
11. Submission of plans for acceptances.	After approval by the judge as fair and equitable, and feasible, plans are transmitted to security holders together with informative materials, including the judge's opinion and the Commission's report (Sects. 174, 175).	

	Chapter X	Chapter XI
12. Solicitation of acceptances.	May not normally be solicited until after judge has approved plan and informative materials have been transmitted (Sec. 176).	May be solicited at any time, even prior to institution of proceeding, and must be obtained before court confirms arrangement (Secs 336 (4), 361, 362). No requirement as to data which must accompany solicitation.
13. Acceptances required for confirmation.	Two-thirds in amount of each affected class of creditors and majority of holders of stock (if debtor is not insolvent) (Sec. 179).	Majority in amount and number of each affected class of unsecured creditors (Sec. 362 (1)).
14. Dissenting classes of creditors or stockholders.	If a class of creditors does not accept by two-thirds in amount, or if a class of stockholders does not accept by a majority, the plan may be confirmed if it provides for such classes adequate protection as prescribed by the statute (Secs. 216 (7), (8), 179, 221).	No comparable provisions.
15. Classes of security holders which plan may affect.	Plan may alter and modify the rights of any class of creditors, secured or unsecured, and of any class of stockholders (Sec. 216).	Arrangement may provide for settlement, satisfaction, or extension of unsecured debts only (Secs. 306 (1), 357).
16. Participation in proceeding by security holders.	Have right to be heard on all matters arising in proceeding (Sec. 206); and may act in person, by attorney, or by agent or committee (Sec. 209).	No comparable provision. A creditors' committee may be selected at or before first meeting of creditors (Sec. 338).
17. Control over representatives of security holders.	Information furnished to court concerning employment and interests of representatives of security holders (such as committees, indenture trustees and attorneys), as well as interests of the persons represented (Secs. 210, 211). The judge is empowered to disregard provisions in authorizations of such representatives or to restrain the exercise of powers which are unfair or contrary to public policy (Sec. 212). Claims or stock acquired by the representatives in contemplation of or during the course of proceeding may be limited to actual consideration paid therefor (Sec. 212).	No comparable provisions.
18. Indenture trustees.	Have the right to be heard on all matters arising in the proceeding (Sec. 206); to file a claim on behalf of all holders of securities outstanding under their indenture (Sec. 198); and to file a petition initiating the proceeding under the chapter (Sec. 126).	No comparable provisions and no mention of indenture trustees.

	Chapter X	Chapter XI
19. Lists of security holders.	Trustee is under a duty to prepare and file lists of security holders (Sec. 164). Other persons in possession or control of such lists or information relevant thereto may be required to disclose the lists or such information (Sec. 165). Although in a proper case the court may direct impounding of the lists, bona fide security holders and indenture trustees have an unqualified right to use and inspect them upon terms prescribed by the court (Sec. 166).	No comparable provisions. Debtor files bankruptcy schedules with petition (Sec. 324).
20. Compensation and allowances.	In addition to allowances to officers of the court, the debtor and petitioners, the judge has broad power to make reasonable allowances of compensation and reimbursement for expenses to the representatives of security holders, including committees and indenture trustees, and to individual creditors and stockholders and their attorneys. (Secs. 241-242.)	The debtor is required to deposit the money necessary "to pay the costs and expenses of the proceedings, and the actual and necessary expenses, in such amount as the court may allow," incurred by a creditor's committee (Sec. 337 (2).)
21. Subsidiary corporations.	A petition by or against a subsidiary corporation may be filed in the same court which has approved the petition by or against the parent corporation. (Secs. 129, 106 (13).)	No comparable provision, and no mention of subsidiaries.
22. Future management.	Plan must contain provisions which are equitable, compatible with the interests of security holders, and consistent with public policy, with respect to the manner of selection of the reorganized company's directors and officers. (Sec. 216 (11)); and identity, qualifications, and affiliations of the persons to be directors and officers must be disclosed and meet same test. (Sec. 221 (5).)	No comparable provision.
23. Charter of reorganized company.	Plan must contain provisions requiring inclusion in the reorganized company's charter of provisions for the prohibition of the issuance of non-voting stock, for the equitable distribution of voting power among the new securities possessing such power, for the election of directors representing preferred stockholders in the event of default in payment of preferred dividends, for the general fair and equitable treatment of securities, and for periodic corporate reports to security holders (Secs. 216 (12)).	No comparable provision.

Office Supreme Court, U.S.

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JOHN F. DAVIS, CLERK

In the Supreme Court of the United States.

OCTOBER TERM, 1964.

No. 35

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

v.

AMERICAN TRAILER RENTALS COMPANY,
Respondent.

AMICUS CURIAE BRIEF OF STATE MUTUAL
LIFE ASSURANCE COMPANY OF AMERICA, THE
GEORGE PUTNAM FUND OF BOSTON AND THE
PUTNAM MANAGEMENT COMPANY, INC.

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In the Supreme Court of the United States.

OCTOBER TERM, 1964.

No. 35

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

v.

AMERICAN TRAILER RENTALS COMPANY.
Respondent

AMICUS CURIAE BRIEF OF STATE MUTUAL LIFE ASSURANCE COMPANY OF AMERICA, THE GEORGE PUTNAM FUND OF BOSTON AND THE PUTNAM MANAGEMENT COMPANY, INC., Appellees in *S.E.C. v. Burton* (1st Cir. No. 6623 Pending) involving American Guaranty Corporation* and owners of senior and subordinated debt and stocks of that debtor constituting about one-eighth of its total capital.

Question Presented Here.

Is a District Court's denial of a motion by the Petitioner Commission under Section 328 of the Bankruptcy Act to

* The official Committee of Creditors of American Guaranty Corporation, the Debtor itself and its Receiver concur in the position argued in this brief. See the separate statement of the Committee of Creditors on page 22, *infra*.

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transfer a reorganization proceeding from Chapter XI to Chapter X an abuse of that Court's discretion where the accepted plan of arrangement for a hopelessly bankrupt corporation turns creditor claims, including those of public investors, into shares of a new corporation organized to take over the debtor's business in which the debtor's stockholders receive for their equity interest about 12% of those shares, restricted in voting, dividend and liquidation rights!

Statement of Facts and Proceedings Below.

American Trailer Rentals Company ("American"), formed in 1958 to operate as part of a trailer rentals system and later growing through mergers in 1961 to become the whole of that system, is the debtor in this case. The trailers in the system, which attached to the rear of automobiles, were rented to the general public by service station operators located throughout the country.

The trailers were originally sold by the debtor to individuals, many of whom were public investors, who then leased them back to the debtor under one of the three following arrangements (R. 3, 152):

- (1) 2% of cost per month for 10 years
- (2) 3% of cost per month for 5 years
- (3) 35% of net rental income

Most of the owners chose either (1) or (2), and these choices, unrelated as they were to actual income, led to the debtor's bankruptcy when the system failed to generate sufficient revenue.

The debtor filed a petition under Chapter XI of the Bankruptcy Act on December 20, 1962. An amended plan of arrangement (R. 4, 149) has been worked out under the terms of that Chapter whereby a new company, Capitol Leasing Corporation ("Capitol"), was formed to carry on the debtor's business.

Under the plan the stock of Capitol is to be distributed to the trailer owners (who will assign their trailers to the new company); unsecured creditors and the stockholders of American in the following manner:

1. Trailer Owners and those who paid for trailers never manufactured (see Footnote 5 of the Opinion in the Court of Appeals, 325 F. 2d 47, 49 (10th Cir. 1963) (R. 154))—one share for each \$2 of their remaining investment, all payments under the lease-back agreements to be treated as a return of capital and the trailer owners to waive all claims for money due or to become due under the lease-back agreements (R. 5, 154)¹.

2. Unsecured Creditors—one share of Capitol for each \$3.50 of debt owed by American, except if a creditor was part of the "management" of American, then one share of Capitol for each \$5.50 of debt (R. 6, 148).

3. Shareholders—107,100 shares for the assignment of the rental network consisting of arrangements with about 500 service station operators throughout the country to keep trailers on their property and rent them to the public (R. 5, 154).

¹ Trailer owners are of course free to keep these trailers and not take part in the Plan. Of the 3,000 trailers involved at the date of the petition (R. 153), about 700 had been so withdrawn and 299 had been exchanged for shares as per item 1 above.

Thus, Capitol's securities are to be issued as follows:

	Claims	Shares in Capitol	Owner- ship in Capitol
1. Trailer Owners			
A. Those expected to exchange approximately 2,000 trailers for shares under Plan ..	\$1,021,932	510,966	58.0%
B. Those ordering trailers never manufactured	200,766	100,388	11.4
C. Shares of Capitol outstanding, all of which were issued for assignment of 299 trailers (R. 5)	176,685	88,332	10.0
			79.4%
2. Unsecured Creditors			
A. Creditors who are not management	76,394.50	21,827	2.5
B. Creditors who are management	288,238.50	52,407 ²	6.0
3. Shareholders—for rental network carried as intangible asset at \$500,000 (R. 153)			
		107,100 ²	12.1
		881,020	100.0%

The Securities and Exchange Commission, acting pursuant to Section 328 of the Bankruptcy Act (11 U.S.C. §728) moved in the United States District Court for the District of Colorado to dismiss the proceedings under Chapter XI unless the debtor amended its petition to comply with Chapter X (R. 8). The District Court, after suggesting certain modifications to the plan of arrangement (which led

² Five-year suspension on voting rights, dividends and rights in liquidation. (R. 148).

to the provision that creditors who were identified with the management of the debtor get only one share of Capitol for each \$5.50 of debt owed to them instead of the \$3.50 rate for other creditors (R. 146, 148)), denied the Commission's motion (R. 144-148), and confirmed the amended Plan. On appeal to the Court of Appeals for the Tenth Circuit, the ruling of the District Judge was unanimously affirmed (325 F. 2d 47; R. 151-161). This Court has granted the Securities and Exchange Commission's petition for a writ of certiorari to the Tenth Circuit.

The petition and accompanying brief and the writ encompass only the propriety of the Circuit Court's action in affirming the denial of the Petitioner's motion in the District Court to transfer the proceedings to Chapter X, (page 2 of the Petition and Question presented p. 2 of Petitioner's Brief in the case). This matter was involved in appeal No. 7392 to the Circuit Court (Footnote 1, R. 152). Neither the petition nor writ in this cause undertakes a review of the other appeal to the Circuit, No. 7474 confirming the modified arrangement. (See Footnote 1, R. 152).

THE INTEREST OF THE AMICUS CURIAE.

The position argued in this brief is that whatever result may be reached in this case now before the Court, it is not, as the Petitioner's brief contends, mandatory to make such a transfer in all cases where public investor creditor interests do not receive complete priority for their claims. This position is crucial in the case on the docket of the First Circuit Court of Appeals, No. 6223, entitled *Securities and Exchange Commission v. Burton* (District Court Opinion *sub nom. In re American Guaranty Corp.*, 221 F. Supp. 961 (D.R.I. 1963)), in which those filing this brief are

parties and which case was brought to this Court's attention in Footnote 5, page 16 of the Petitioner's petition for a writ of certiorari in this case at bar.

We urge that should the Court rule in favor of the Petitioner on this appeal, that it make plain its decision is not controlling in the *Burton* case where, under the plan of arrangement there presented, the creditors have complete control of the debtor until all debts are paid in full and the only priority denied public investor creditors and other creditors is at most a two-year interest moratorium on their claims, thus making the facts in that case as to the nature of and effect upon public investor creditor interests very different from those in the present case.

Statutes Involved.

Bankruptcy Act:

Chapter X, Section 130 (11 U.S.C. §530)

Every petition shall state— . . .(7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter 11 of this title; . . .

Chapter X, Section 147 (11 U.S.C. §547)

Amendment of Petition to Comply with Provisions Governing Arrangements

A petition filed under this chapter improperly because adequate relief can be obtained by the debtor under chapter 11 of this title may, upon the application of the debtor, be amended to comply with the requirements of chapter 11 for the filing of a debtor's petition, and shall thereafter for the purposes of chapter 11 be deemed to have been originally filed thereunder.

Chapter XI, Section 328 (11 U.S.C. §728)***Dismissal, Proceedings; Amended Petition***

The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter.

Chapter XI, Section 366 (11 U.S.C. §766)***Requisites for Confirmation***

The court shall confirm an arrangement if satisfied that —(1) the provisions of this chapter have been complied with; (2) it is for the best interests of the creditors and is feasible; (3) the debtor has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of a bankrupt; and (4) the proposal and its acceptance are in good faith and have not been made or procured by any means, promises, or acts forbidden by this title.

Confirmation of an arrangement shall not be refused solely because the interest of a debtor, or if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement.

Summary of Argument.

Bankruptcy Act, Section 328, under which was made the Petitioner's motion to transfer a Chapter XI proceeding to Chapter X gives the District Judge discretion, not to be reversed unless its exercise was "beyond allowable bounds." There has been no showing that adequate relief cannot be obtained in Chapter XI for this financially distressed corporation with only unsecured debt. This Court has stated that the presence of public investor creditors does not preclude use of Chapter XI and preservation of stock interests is clearly permitted by Section 366 of the Bankruptcy Act. The deletion of the "fair and equitable" requirement for Chapter XI plans by 1952 amendments means that absolute priority of creditors over equity interests is no longer essential to a plan of arrangement. The proper statutory test is only whether the plan is "in the best interests of creditors and feasible." There is no review presented here of the rulings that the plan in this case met these requirements. The denial of the ~~transfer~~ motion was not "beyond allowable bounds."

In *Securities and Exchange Commission v. Burton* (First Circuit No. 6223 Pending), where those submitting this *amicus curiae* brief are appellees, the only denial of absolute priority for public investor creditors involves a two-year waiver of interest. An independent receiver is in possession, and public investors are as protected as they would be in a Chapter X proceeding and will receive more than in a liquidation.

Any ruling that this Court may make in favor of the Petitioner in this case at bar should not effect the question presented in the *Burton* case where the facts are substantially different from those at bar.

Argument.

I. A DISTRICT COURT IS NOT REQUIRED TO TRANSFER A REORGANIZATION CASE FROM CHAPTER XI TO CHAPTER X OF THE BANKRUPTCY ACT WHERE A PLAN OF ARRANGEMENT PROVIDES SHARES IN A NEW CORPORATION FOR ALL CREDITORS, INCLUDING PUBLIC INVESTORS, ON A SCALED DOWN BASIS LEAVING SHAREHOLDERS OF THE DEBTOR ABOUT 12% OF THE NEW CORPORATION'S SHARES WITH RESTRICTED VOTING, DIVIDEND AND LIQUIDATION RIGHTS.

This Court has decided in *General Stores Corp. v. Shlen-sky*, 350 U.S. 462 (1956), that the general test against which the discretionary action of a District Court hearing a Section 328 motion is to be measured is "the needs to be served" (350 U.S. at 468). The application of this "Delphic" test and principle to the facts of each case may well reach different results in different cases, and this was recognized in *General Stores, supra*, where it was pointed out that:

[a] large company with publicly-held securities may have as much need for a simple composition of unsecured debts as a smaller company. (350 U.S. at 466)

From this language and from the opinion in *In re Grayson-Robinson Stores, Inc.*, 215 F. Supp. 921, 935 (S.D.N.Y. 1963), aff'd *sub nom. Grayson-Robinson Stores, Inc. v. Securities and Exchange Commission*, 320 F. 2d 940 (2d Cir. 1963), the Circuit Court in the case at bar quite properly concluded that the "mere existence of public investors does not preclude use of Chapter XI." (325 F. 2d at 50) (R. 156)

The controlling statutory word, "may" in Section 328, "surely not the strongest auxiliary verb in the language", (*Grayson-Robinson Stores, Inc. v. Securities and Exchange*

*Commission, *supra*, 320 F. 2d at 948), is one giving the lower court discretion, reversible as noted above only if the action "transcended allowable bounds." (*General Stores Corp. v. Shlensky, supra*, 350 U.S. at 468).

The Petitioner takes the position that corporate reorganizations under Chapter XI may not scale down in any manner the creditor priority of public investors. The contention is that District Judge has no discretion but is required to transfer to Chapter X on a motion under Section 328 any proceeding under Chapter XI attempting to limit claims of the public and preserve the interests of the stockholders. This is in contradiction of the clear discretionary language of Section 328 and the language of Section 366 which provides:

... Confirmation of an arrangement shall not be refused solely because . . . the interests of [the debtor's] stockholders or members will be preserved under the arrangement. (11 U.S.C. §766)

Four District Courts have recently held the Commission's contention fallacious and refused to order transfers.³ The facts of each case may well warrant different results, but under the present Chapter XI there is no absolute requirement that a transfer be ordered whenever public investor creditors do not receive full and strict priority. The narrowing of this above-noted statutory discretion by judicial fiat has no proper place in these proceedings.

³The District Court of Colorado in this case; *In re American Guaranty Corp.*, 221 F. Supp. 961 (D.R.I. 1963) appeal pending *sub nom. Securities and Exchange Commission v. Burton* (1st Cir. No. 6623); *In re Crumpton Builders, Inc.* (M.D. Fla. No. 63-4-2T) appeal pending *sub nom. Securities and Exchange Commission v. Crumpton Builders, Inc.* (5th Cir. No. 20712); and *In the Matter of Canandaigua Enterprises Corp.* (W.D.N.Y. 1964) appeal pending (2nd Cir. No. 29012)

A basic consideration in the case at bar is whether or not a plan of arrangement under Chapter XI is for the best interests of creditors where the former stockholders, some of whom had also made loans to the company in addition to their equity investment, receive an 18% stock interest in the reorganized company (12% from their equity interest including the rental system and 6% from loans on a scaled-down basis much more drastic than that applied to other creditors), this stock interest to be non-voting and without dividends for five years (R. 148). Such a plan can perfectly well be fair and equitable and definitely in the best interests of creditors if the alternative is liquidation in bankruptcy or under expensive Chapter X. See the next to last paragraph in the Circuit Court's Opinion in this case (325 F. 2d at 53, R. 161) and *In re Village Men's Shops, Inc.*, 186 F. Supp. 125 (S.D. Ind. 1960), which note that "in the best interests of creditors" means broadly that a Chapter XI plan is to be preferred if it yields more to the creditors than would a liquidation. See also *Bartle v. Markson Bros., Inc.*, 314 F. 2d 303 (2d Cir. 1963), in which, while reversing the confirmation of a plan on other grounds, the court (Clark, J.) stated:

Since, however, the amount to be received under the plan of arrangement compares favorably with probable liquidation payments and since the creditors were fully informed in advance, we do not regard the referee's finding the arrangement was in the best interests of the creditors as necessarily erroneous in law. (314 F. 2d at 305)

⁴ The phrase "in the best interest of the creditors" is the same phrase in former Section 12d of the Bankruptcy Act before the revision of 1938 and it was interpreted:

. . . to require a comparison between what creditors would receive under the composition offer and what they would receive in a liquidation of the estate. . . . Where creditors would not realize as much in liquidation as they would receive under the composition offer, or where it is uncertain that liquidation would result in any appreciable advantage over the composition offer, the composition under §12 was for the best interests of creditors. 9 Collier on Bankruptcy, (14th Ed.) §9.17, pp. 280-281.

Chapter X by the express words of Section 130(7) (11 U.S.C. §530(7)) applies only when by specific facts it is shown "why adequate relief cannot be obtained under Chapter XI." This and the provision of Section 328 that transfer depends upon a finding that "the proceedings should have been brought under Chapter X" show that Chapter XI is the normal avenue for relief of a distressed corporation with only unsecured debt.

This analysis is further confirmed by the provisions of Section 147 of Chapter X (11 U.S.C. §547) providing for the transfer to Chapter XI of a Chapter X proceeding on the grounds that "adequate relief can be obtained by the debtor under Chapter XI."

The Petitioner's real complaint here is that the plan is not on Chapter X standards fair to the public investor creditors (the trailer owners). This is not the question here. The proper way to raise that issue is on a review of the order confirming the plan. The S.E.C. did intervene to do this as in *In re Lea Fabrics*, 272 F.2d 769 (3rd Cir. 1959). The appeal from such an order, not presented in this case, directly raises the question of whether the plan met the requirement that it was "for the best interests of creditors and is feasible." This type of procedure is well illustrated in *Bartle v. Markson Bros., Inc.*, 314 F.2d 303, *supra*, where the plan was disapproved on an appeal by creditors because there had been no proper explanation of missing assets.

The appeal (C.C.A. No. 7474; R. 152) from the confirmation decree, which is not covered by the certiorari writ as above noted, raises directly the issue of best interests of creditors of all kinds and brings all facts under review, whereas this appeal from a denial of the motion under Section 328 really does not involve the question of the

plans' compliance with the requirements for confirmation in Sec. 366(2) (11 U.S.C. §766(2)).

This becomes very clear when one realizes there is no Congressional intent shown to exclude this type of case from Chapter XI; that under Chapter XI debtors can be helped if the plan of arrangement is "in the best interests of creditors," an appealable determination; and that the cumbersome procedures of Chapter X involving much time and money afford no better basis for action by the S.E.C. than its intervention in a Chapter XI proceeding to determine whether the plan is "in the best interests of creditors," large and small, public and private.

In the case at bar, with all creditors on an unsecured basis, except about \$10,000 of priority tax items and a chattel mortgage, there is nothing to indicate "adequate relief cannot be obtained" in a Chapter XI proceeding. If there is in fact something objectionable about the proposed reorganization, surely it is in the proposed plan of arrangement rather than in the use of Chapter XI as the avenue of reorganization.

On this analysis also the Petitioner's argument in Point B, pp. 39 to 49 of its brief is ineffective on the question presented and subject to review here under the granted writ.

This question of the propriety of the preservation of stockholder interests is quite independent of other issues of mismanagement, violation of the Securities Act of 1933 in the distribution of securities and other separate possible disciplinary action which the Commission might feel called upon to take. These other issues should not obscure or affect the decision on the only question which is covered by the certiorari writ in this case.

The cumbersome proceedings and S.E.C. report involved in a Chapter X proceeding are not necessary to protect creditors. Congress delegated that duty to the judge in Section 366 (2) (11 U.S.C. §766(2)) by providing that before confirmation he must find the plan "in the best interests of creditors," which, of course, includes the trailer-owner public investor in this case. This necessity for court approval is a statutory protection actually exercised in this case by the District Judge (R. 146), who required changes in the rate at which shares of the new corporation were issuable, so that management people who were creditors received far less for their claims than other creditors.

The Petitioner's principal reliance is upon the so-called rule of strict priority which would appear in this case to mean that none of the shares of the new company could under the plan be distributed to former shareholders. This strict priority principle emanates from *Northern Pacific Railway Co. v. Boyd*, 228 U.S. 482 (1913), but it "does not . . . require . . . [payment of] unsecured creditor[s] in cash as a condition of stockholders retaining an interest" (228 U.S. 508). The *Boyd* case did not involve any federal Act under which creditors' rights were affected by statute. It was a voluntary change by a controlling stockholder who caused a foreclosure which cut off a judgment creditor; *Boyd*.

The other case which stands at the root of the so-called strict priority rule is *Case v. Los Angeles Lumber Products Company, Ltd.*, 308 U.S. 106 (1939). There a confirmed plan under old Section 77B was reversed because shareholders of the debtor "insolvent both in the equity and bankruptcy sense, with no indicated equity received 23% of the vote in the reorganized company." The court held that the words "fair and equitable" in Section 77B re-

quired that absolute priority be given the claims of creditors, although the court acknowledged that this requirement did not have to be met by a cash payment (308 U.S. at 116, 117).

The principle of those cases no longer applies to a Chapter XI proceeding. Congress, by the 1952 Amendments to Section 366 of the Bankruptcy Act (11 U.S.C. §766), deleted the former requirement of "fair and equitable", so that the plan need now be only "for the best interests of creditors" and "feasible." Had there been any intention on Congress's part to provide that, under a plan, stockholders may not receive anything until the creditors are paid in full, the 1952 Amendments would certainly have not inserted the last clause of Section 366 which specifically provides that retention of a stockholder's interests is proper under a Chapter XI plan.

The Commission argues to the contrary that the 1952 deletion of the words "fair and equitable" was merely a "qualifying" and "uncontroversial" amendment intended to do no more than allow the scaling down of trade creditors' claims without any change in the claims of junior securities holders. It is difficult to understand how the Commission may argue at one point that "fair and equitable" are words of art, importing the definite and fixed requirement of absolute priority and at another point that the deletion of this phrase from the statute is not intended to affect the substantive requirements the words have been construed to import.⁵

⁵ These Amendments were far from "uncontroversial" as indicated by the examples in 9 Collier on Bankruptcy (14th Ed.) §9.18(2.1) pp. 304-305; and H. R. Rep. No. 2320, 82nd Cong., 2nd Sess., p. 21 (1952); 1952 U.S. Code Cong. & Admin. News. pp. 1981-82 (objection of Treasury Department).

There is absolutely nothing in Chapter XI or the 1952 Amendments which suggests, as the Petitioner argues, the use of the chapter is limited to arrangements with trade creditors.

The legislative history of the 1952 Amendments indicates very clearly that their purpose was to do away with notions of absolute priority in Chapter XI proceedings. In H. R. Rep. No. 2320 (the Committee Report on the basis of which the 1952 Amendments were enacted), 82nd Cong., 2d Sess., p. 21 (1952), it was stated:

In fact, however, the fair and equitable rule as interpreted in *Northern Pacific Railway v. Boyd*, 228 U.S. 482; (*supra*) and *Case v. Los Angeles Lumber Products Co., Ltd.*, 308 U.S. 106, (*supra*) cannot realistically be applied in a Chapter XI, XII or XIII proceeding.

The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the *Boyd* and *Los Angeles* cases shall not be operative under those three chapters. U.S. Code Cong. & Admin. News, 1952, pp. 1981, 1982

These Amendments can have no other significance than that Congress intended Chapter XI to be available to all types of corporations with only unsecured debt which are in trouble, excluding only those where it should be shown that adequate relief could not be obtained under Chapter XI. Had there been any intention to exclude corporations with public investor creditors or those where stockholders were left with some interests under the plan, it would have been very easy for Congress to say so. These Amendments make clear that the judicial rule of strict priority enunciated years ago under the peculiar circumstances of the

Boyd case, *supra*, has no bearing on plans of arrangement which were "feasible." Though "strict priority," i.e., payment in full before junior claims get anything, may sometimes be a factor in making a plan "feasible," it is not today a requirement for confirmation of a Chapter XI plan.

The purpose of this review is to have this Court engraft upon the statute an exception in cases where some of the creditors are public investors. As authority for this proposition of absolute priority for public investors, the Commission points to language in the case of *General Stores Corp. v. Shlensky*, *supra*, where the Court gave the following as one of several examples of when Chapter X was more suitable than Chapter XI:

Readjustment of all or a part of the debt of an insolvent company without sacrifice by the stockholders may violate the fundamental principle of a fair and equitable plan. (Citing two cases decided before the amendments to Section 366) (350 U.S. at 466)

It is the Commission's contention that this language represents a holding by the Supreme Court that there still must be absolute priority for the claims of public investor creditors in any plan of arrangement, despite the Amendments to Section 366. If this is true, then absolute priority is still the rule as to claims of all creditors (including trade creditors), since the language used by the court makes no distinction in the kind of creditors entitled to a "fair and equitable" plan. The result of this would be that the amendments to Section 366 were absolutely meaningless.

The Commission's argument that creditors must still receive absolute priority despite the amendments to Section 366 relies almost solely on this broad hypothetical illustration without delving into the factual or stylistic context of

the case in which it was given. In the first place, notwithstanding the Commission's contention to the contrary, the Supreme Court has never given full consideration to the 1952 Amendments to Section 366.⁶ Secondly, a careful reading of the quotation will show that it is inappropriate in a case where the stockholders, by the terms of a plan of arrangement, also make sacrifices in order to aid in the rehabilitation of the debtor. Thus, in the case at bar the stockholders are giving up their complete ownership of the debtor to become minority shareholders in the new corporation without vote or dividends for five years. Also, management shareholders who have unsecured debts owed by the corporation are receiving for those debts about half of what other unsecured creditors receive. Further sacrifices by management shareholders include a five-year suspension on voting rights, dividend rights, and rights in liquidation (R. 148).

Also, it should be noted that the language in the quotation is permissive—readjustment without sacrifice by stockholders “may violate the fundamental principle of a fair and equitable plan.” Finally, the court merely states that in such a hypothetical circumstance, “Chapter X affords a more adequate remedy than Chapter XI,” which is not the same thing as saying that Chapter XI is inadequate or that it is an abuse of discretion of the District Judge to refuse a transfer to Chapter X. In this context it must be remembered that the Court in *General Stores* was reviewing the decision of lower courts granting a motion to transfer

⁶“Since the *Realty* decision to no small degree turned on the enforcement of the ‘fair and equitable’ rule, it is noteworthy that no consideration was given by the lower courts, and none is given by this court, to the significance of this amendment by Congress.” Frankfurter, J., dissenting in *General Stores Corp. v. Shlensky*, *supra*, 350 U.S. at 472 (1956)

proceedings to Chapter X rather than the denial of such a motion.

It is therefore respectfully urged that the decision of the Circuit Court be affirmed.

II. THE DECISION IN THIS CASE SHOULD GO NO FURTHER THAN TO DEAL WITH THE PARTICULAR FACTS PRESENTED, BECAUSE IN THE BURTON CASE NOW BEFORE THE COURT OF APPEALS FOR THE FIRST CIRCUIT, THE ONLY SACRIFICE BY PUBLIC INVESTOR CREDITORS IS AT MOST A TWO-YEAR WAIVER OF INTEREST ON THEIR CLAIMS AND BECAUSE THE PLAN IN THAT CASE PROVIDES SAFEGUARDS SIMILAR TO THOSE FOUND IN CHAPTER X, MAKING THAT CASE FAR DIFFERENT IN SPIRIT AND IN LAW FROM THE CASE AT BAR.

The above considerations are particularly applicable to the First Circuit case in which those submitting this brief are parties. In that case a Receiver is in possession of the debtor, and the plan of arrangement envisages his control in distributing funds during the time until all creditors are paid in full, except for a waiver of interest pending judicial proceedings not in excess of two years.

In the *Burton* case the stockholders have no voice in the operation of the business or its further development without creditor assent until all creditors are paid, except for a limited veto subject to arbitration on sales of assets in excess of \$20,000. It would be most unfair to force the debtor in that case, American Guaranty Corporation, into Chapter X simply because of the waiver of interest negotiated for the benefit of public investors holding subordinated debt and stocks.

The two-year time limit on this waiver, which was necessary only because of the delays inherent in court pro-

cedures, is not a serious flaw in a plan even on a strict priority basis, because it is only reasonable that the interest cost resulting from such inevitable court delays in processing this type of situation should not be borne entirely by the stockholders and junior creditors (many of whom are small public investors). Other substantial expenses of negotiation, administration and litigation do come from funds that would otherwise be available for publicly held subordinated debt and stocks. That is enough burden for these interests to bear, and it is eminently fair that the interest waiver put a part of the arrangement expense upon the senior creditors. In short, the plan in the *Burton* case is both "fair and equitable" and not contrary to any rule of strict priority. However, it is urged that the plan is not required to conform to any such rule.

Reliance by the Petitioner on certain provisions of Chapter X, notably those with regard to an independent trustee's developing the plan of reorganization and an S.E.C. investigation and report as provided for in Sections 156, 158, 167, 174 and 175 of Chapter X (11 U.S.C. §§556, 558, 567, 574 and 575) are not criteria for a holding that a District Judge abused his discretion under Section 328 (11 U.S.C. §728) because in the *Burton* case: (1) an independent receiver is in possession with qualified counsel and power to enforce the corporation's claims for mismanagement; (2) under the direction of the referee an investigation of possible misdeeds in line with the provisions of Section 21(a) of the Bankruptcy Act (11 U.S.C. §44(a)) is now current; (3) the Petitioner, as an intervenor, can participate in the necessary determination by the referee and the court just as effectively as in a Chapter X proceeding; (4) the independent receiver charged with the duty of collecting assets can prosecute just as effectively as an inde-

pendent trustee causes of action belonging to the estate; and (5) the plan of arrangement was prepared and developed in large measure by the creditors, not the debtor.

In connection with (2) above, see *Grayson-Robinson Stores, Inc. v. Securities and Exchange Commission, supra*, 320 F. 2d 940 (2d Cir. 1963), in which Judge Friendly stated that if there is a Section 21(a) investigation and the S.E.C. does not particularize in what respects this investigation is not complete, then, although a Section 21(a) investigation may not be as thorough as one by a trustee under Chapter X, it can be said that the District Judge:

... properly looked at what had already been done and what may be done in the future in determining whether the benefits of a Chapter X investigation would outweigh the detriments of transfer to that chapter. (320 F. 2d 949)

The appendix to this brief shows that the Chapter X protective provisions relied on by the Petitioner in arguing transfer to that Chapter have been incorporated into the modified plan of arrangement in the *Burton* case, so that the comparative summary of Chapter X and Chapter XI processes in the Appendix to Petitioner's brief cannot show in the *Burton* case any inadequacy of the plan because of an alleged lack of protective provisions.

The Commission is attempting to engraft an absolute priority requirement on all Chapter XI proceedings involving public investor creditors by means of the following syllogism:

1. The *Boyd* and *Los Angeles* cases say all corporate rehabilitations must give absolute priority to the claims of creditors.

2. Congress deleted from Chapter XI the "fair and equitable" provision upon which was based the absolute priority requirement.

3. Therefore, Chapter XI cannot be used if it violates the rule of *Boyd* and *Los Angeles* (at least when the creditors are public investors).

Patently, the above construction does not hold water. No. 3 should read: "Therefore, the rule of *Boyd* and *Los Angeles* no longer applies to Chapter XI arrangements."

To a certain extent the Commission has succeeded in its efforts. It has been noted in *Collier on Bankruptcy*:

There is, however, some indication that the 'fair and equitable' test may be reintroduced in Chapter XI by indirection. Suggestive of this are several cases which, in ruling that the proceeding involved should have been brought under Chapter X rather than Chapter XI, gave as a reason not only that there was need of independent and thorough analysis by a court or trustee but also that a scaling down of the claims of creditors without some compensating advantage to them which is prior to the rights of stockholders would prevent a fair and equitable arrangement from being consummated under Chapter XI. 9 *Collier on Bankruptcy* (14th Ed.) Para 9.18(2.1) at 306

The author concludes, however:

Since the legislative elimination of the 'fair and equitable' test, use and reliance on these words in view of the past interpretation, should not be continued. While several decisions have continued to refer to the 'fair and equitable' test, other and sound reasons for favoring Chapter X of Chapter XI were present in those cases. *Ibid.*

Statement of Committee of Creditors.

The official Committee of Creditors of America Guaranty Corporation, the Debtor involved in the case of *Securities*

and Exchange Commission v. Burton, now pending before the Court of Appeals for the First Circuit (Docket Number 6223) concurs in the position argued in this *amicus curiae* brief. It believes that the needs-to-be-served criteria developed under this Court's decision in *General Stores Corp. v. Shlensky*, 350 U. S. 462 (1956), have provided the United States District Courts with the requisite flexibility to prescribe remedies for the extraordinary variety of economic ills which can and do beset corporate debtors. The rigid position now urged by the Petitioner is not a satisfactory or practical alternative for a discriminating determination of appropriate relief in each particular case. See Weintraub & Levin, "Reorganization or Arrangement: An Analysis of Contemporary Trends in Recent Cases," 1963 *Journal Nat'l. Ass'n. Referee in Bankruptcy* 103.

III. CONCLUSION.

For the reasons stated above, the Court should not rule that Congress intended in a Chapter XI arrangement that absolute priority must be given the claims of public investor creditors, so that, if the arrangement attempts so to deny absolute priority, *ipso facto* the proceeding should be dismissed or transferred to Chapter X. Rather the Court should examine the bankrupt corporation and the claims of its creditors to determine whether Chapter XI meets the "needs to be served."

Four judges have so determined and confirmed the plan as "in the best interests of creditors and feasible", and the confirmation is not under review here. Certainly on the basic question at bar it is clear that the District Judge was not too wide of the mark, or guided by such faulty standards, that his judgment in refusing a transfer to Chapter X was an abuse of discretion.

It is our position and hope that in its decision in this case the Court lay to rest the Securities and Exchange Commission's illogical position: that the elimination of "fair and equitable" from Chapter XI makes that Chapter unsuitable whenever an arrangement under it denies in any way absolute priority to the claims of public investor creditors.

Consequently, we urge that the decision in this case should not touch a Chapter XI proceeding such as is presented in the *Burton* case.

Respectfully submitted,

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September 18, 1964

Appendix.

The Petitioner contends that public-investor creditors can only be adequately protected by proceeding under Chapter X. As the following table shows, this is not necessarily so. In the plan of arrangement under Chapter XI of American Guaranty Corporation involved in *Securities and Exchange Commission v. Burton* (1st Cir. No. 6623) provisions substantially identical to the protections afforded by Chapter X have been included.

<i>Item from Petitioner's Comparison and Description</i>	<i>Substantially Identical Provision in American Guaranty Corp. Plan of Arrangement</i>
1-3. Independent Trustee.	Independent Receiver in possession.
4-6. Examination and reports on Debtor's Finances and Conduct.	Referee's designee Charles J. McGovern, Esq., of the Providence Bar to investigate in line with Section 21(a) of the Bankruptcy Act (11 U.S.C. §44(a)) and report to S.E.C., creditors and stockholders (Art. V C).
7-8. Formulation and filing of Plan by Trustee.	Plan developed after careful negotiations with help of the Referee between Debtor, creditors and stockholders, each represented by independent counsel.
9. Assistance of S.E.C.	S.E.C. is a party, having been permitted to intervene.

10-12. Nature of Plan and Submission.	Plan developed with assistance of Referee; transmitted to creditors subject to finding of "best interests of creditors."
13-14. Acceptances.	Much more than two-thirds of creditors have approved and stock rights suspended but not permanently affected (Art. II C).
15. Classes affected.	Only unsecured debts involved.
16. Participation in proceeding.	Many have entered appearances and have been heard.
17. Control of representatives.	Creditor executive committee to have Referee approval.
18-23. Elements concerning: Indenture Trustees, Lists of Security Holders, Compensation and allowances, Subsidiary Corporations, Future Management, and the charter of the Reorganized Company.	These elements are either not of a "protective nature," or they are available, or there is provision for Referee or Court approval.

Consents to Filing of Amicus Curiae Brief.

Dear Mr. Jenckes:

As requested in your letter of August 5, 1964, I am happy to consent to the filing in the above case of a brief *amicus curiae* on behalf of the State Mutual Life Assurance Company of America, The George Putnam Fund of Boston and the Putnam Management Company, Inc. As discussed in our previous correspondence, my consent also extends to the joining in such brief of the Creditors' Committee that is a party in the pending case of *Securities and Exchange Commission v. Burton*, C.A. 1, No. 6223.

There is inclosed an extra copy of this letter, so that you can file the original with your brief, as required by Rule 42(2) of the Revised Rules of the Supreme Court.

Sincerely,

/s/ ARCHIBALD COX

ARCHIBALD COX
Solicitor General

American Trailer Rentals Company, the above-named respondent, consents to the filing of a brief of an *amicus curiae* on the merits in the above entitled matter by Marcien Jenckes, Esquire, of Choate, Hall & Stewart, Boston, Massachusetts. This consent is given pursuant to Rule 42(2).

AMERICAN TRAILER RENTALS COMPANY
By /s/ ARTHUR W. BURKE, JR.

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Attorney for Respondent,
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Office-Supreme Court, U.S.

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IN THE

SUPREME COURT OF THE
UNITED STATES

October Term, 1964

No. 35

SECURITIES AND EXCHANGE COMMISSION,
Petitioner

v.

AMERICAN TRAILER RENTALS COMPANY,
Respondent

ANSWER BRIEF OF
AMERICAN TRAILER RENTALS COMPANY

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October Term, 1964

No. 35

SECURITIES AND EXCHANGE COMMISSION,
Petitioner

v.

AMERICAN TRAILER RENTALS COMPANY,
Respondent

ANSWER BRIEF OF AMERICAN TRAILER RENTALS COMPANY

QUESTION

Do the lower courts have discretion to determine whether a Chapter XI arrangement meets the public and private needs to be served where certain creditors, owners of trailers leased to debtor, have been asked to exchange their trailers for stock, on a completely voluntary basis, and where all other creditors, including stockholders' equity claims, are settling their claims for stock, or is such arrangement prohibited by some restriction in the Bankruptcy Act?

STATUTES INVOLVED

Bankruptcy Act:

Chapter XI, Section 366 (11 U.S.C. §766).

"Requisites for Confirmation"

"The court shall confirm an arrangement if satisfied that — (1) the provisions of this chapter have been complied with; (2) it is for the best interests of the creditors and is feasible; (3) the debtor has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of a bankrupt; and (4) the proposal and its acceptance are in good faith and have not been made or procured by any means, promises, or acts forbidden by this title.

"Confirmation of an arrangement shall not be refused solely because the interest of a debtor, or if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement."

Chapter XI, Section 328 (11 U.S.C. §728)

"Dismissal Proceedings; Amended Petition"

"The judge may, upon application of the Securities and Exchange Commission, or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for

the filing of a debtor's petition or a creditors' petition under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter."

Chapter X, Section 130 (11 U.S.C. §530)

"Every petition shall state — . . . (7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter 11 of this title; . . ."

Chapter X, Section 147 (11 U.S.C. §547)

"Amendment of Petition to Comply with Provisions Governing Arrangements"

"A petition filed under this chapter improperly because adequate relief can be obtained by the debtor under chapter 11 of this title may, upon the application of the debtor, be amended to comply with the requirements of chapter 11 for the filing of a debtor's petition, and shall thereafter for the purposes of chapter 11 be deemed to have been originally filed thereunder."

STATEMENT OF FACTS

American Trailer Rentals Company was organized in 1958 in Denver, Colorado. (R. 3) Its primary purpose was the rental of utility trailers to the public through a system of trailer rental stations throughout the United States.

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(R. 3) For the most part these rental stations are gasoline service stations, which, at one time numbered 700. At the time of the filing of Chapter XI, the number of stations was approximately 500. (R. 3)

The trailers are utility trailers rented by the public for various personal purposes, from the hauling of trash to the moving of furniture cross country. The trailers were leased to the company for this use for the most part for 2% of the cost of the trailer¹ per month for 10 years by the owners.² The trailers were sold to the owners by various state sales companies in the states involved, and upon manufacture a title to the trailer (as in the case of a motor vehicle) was issued by the titling states, in the name of the trailer owner, which title was delivered to the owner and retained by him. All of the state sales companies operated by virtue of a contract with Executive Sales Company since merged into the debtor. A simultaneous lease was executed by these owners with a state rental company located in the state where the trailers were purchased, which state companies then turned the actual operation of the trailers over to American Trailer Rental, Company by virtue of an operating agreement. These state companies, for the most part, have been merged into the debtor. (R. 131) The price of the trailer included a commission out of which the state sales companies retained 20% of the sales price, and Executive Sales Company received an amount equal to between 5% and 17% of the sales price.³ (R. 74)

¹A small portion were leased for 3% per month for 5 years and some for 35% of gross rentals.

²These leases were not related to the income of the system and created the primary financial problem of the company.

³From the amount received by Executive Sales Company, certain loans were made to the debtor which funds were used for the general purposes of the debtor. (R. 76) The debt from the debtor to Executive was balanced with a debt due from Executive to American and the merger between American and Executive was on a straight stock basis.

The balance of the purchase price was paid by Executive Sales Company to the manufacturer for the manufacture of each trailer.

At the peak, the company had 5,868 trailers committed to its fleet although at the peak period of operation there were only about 3,000 trailers actually operating in the system. (R. 118) The management of the company has been in three different groups from the commencement of the operation until the present date. (R. 121-122) The first two management groups were replaced and the third, or present group, came into actual control of the debtor in July of 1960. They have attempted by various direct means to resolve the problems of the company but have been unable to do so. (R. 112)

On April 12, 1961, and thereafter, the Securities and Exchange Commission engaged in an investigation of the company and the company was advised by the Securities and Exchange Commission that the Securities and Exchange Commission believed this overall program constituted a sale of a security.⁴ The company thereafter commenced preparation for filing of a registration statement. It had been advised by the Securities and Exchange Commission that a financial statement need not be completely certified and it thereafter filed a registration statement. (R. 82) This registration Statement was filed on December 11, 1961. (R. 22) The company heard nothing on the attempted registration until November 27, 1962 (R. 17) at which time the Securities and Exchange Com-

⁴Quite the contrary from the statement in the Securities and Exchange Commission's brief, the company was never advised why this was believed to be a security, just that it was believed to be a security and to stop sales or be stopped.

⁵The uneconomical leases on the trailers did not constitute the only claim on the company revenue. The compliance with Securities and Exchange Commission requirements subsequent to April 12, 1961, also created financial problems for the company. (R. 112)

mission issued a temporary order suspending the effectiveness of the registration which had never become effective.

After the investigation by the Securities and Exchange Commission and numerous conferences with the commission staff, some of the trailer owners, together with the vice president of the debtor, formed a company called Capitol Leasing Corporation and, relying on the Regulation A exemption of the Securities Act of 1933, made an offer to the trailer owners of American offering to exchange stock in Capitol for their trailers at the rate of one share of stock for every \$2 invested in the trailers to be exchanged. On October 9, 1962, the Securities and Exchange Commission suspended this offering and a hearing has been had on this matter.

On December 20, 1962, the company, faced with un-economic leases and no way to resolve the dilemma, with mounting monthly obligations which could not be met, filed the subject Chapter XI.

THE PROPOSED ARRANGEMENT

The arrangement proposed by American anticipates the issuance of common stock of Capitol Leasing Corporation, a Colorado corporation, in satisfaction of the obligations of American on the following basis:

1. Capitol Leasing Corporation will issue one share of its stock to trailer owners for each \$2 of remaining capital investment in exchange for title to the subject trailers. Remaining capital investment is determined by deducting from sales price of the trailers the amount paid by American to trailer owners (including certain trailer

owners whose trailers were never manufactured due to bankruptcy of the manufacturer.)

2. Capitol Leasing Corporation will issue one share of its stock for every \$3.50 of claim of general creditors.

3. Capitol Leasing Corporation will issue one share of stock for every \$5.50 of claim for loans by stockholder-creditors to American. These shares also carry restrictions on voting (one vote for every seven shares of stock) and no participation in dividends or liquidation for five years.

4. Trailer owners who do not elect to participate in the plan may take possession of their trailers.

As an adjunct of the plan, Capitol Leasing Corporation proposes to buy the operating system of American for 107,100 shares of its stock.

Presuming that 2,000 trailers are exchanged for stock under the plan, the following is a breakdown of the stock of Capitol Leasing Corporation upon completion of the plan:

	<i>Shares in Capitol</i>	<i>Ownership</i>
1. Trailer owners who exchanged for stock	510,966	58.0%
2. Trailer owners whose trailers were not manufactured	100,388	11.4%
3. Shares of Capitol heretofore exchanged for trailers	176,665	10.0%
TOTAL SHARES ISSUED FOR TRAILERS		79.4%

*Shares in
Capitol Ownership*

TOTAL SHARES ISSUED FOR TRAILERS 79.4%

4. Creditors excluding share-holders	21,827	2.5%
5. Creditors who are shareholders	52,407¹	6.0%
6. Shareholders	107,100	12.1%
		<hr/>
		100.0%

The Securities and Exchange Commission filed a motion under Section 328 of Chapter 11, Bankruptcy Act (11 U.S.C. §728) demanding dismissal of the proceedings. This motion was heard by the Chief Referee in Bankruptcy for the District of Colorado, as Master, who recommended denial of the motion. The district court adopted the Master's findings and on appeal, the court of appeals affirmed the lower court.

SUMMARY OF ARGUMENT

In the proposed Plan, we are dealing with an arrangement which has survived attack by the Securities and Exchange Commission before three separate judicial bodies — the Chief Referee in Bankruptcy, the presiding Judge of the District Court for the State of Colorado, and the United States Court of Appeals for the Tenth Circuit; which has been accepted by the majority in number of claims filed and the majority in dollar amounts of claims.

¹The plan originally proposed to issue one share of stock for every \$3.50 of these claims but was amended to reduce the participation of these claimants. The plan was also amended to reduce voting rights to one vote for every seven shares owned, with no participation in dividend or liquidation for five years.

filed; which has been found to be feasible and in the best interests of creditors by the four judges and Referee before whom the matter has previously been litigated; and which has been confirmed on May 23, 1963.

For the case at bar the proposed Chapter XI arrangement provides the simplest, most feasible and probably the only workable method of meeting the needs to be served. The plan which is herein proposed provides for continuous operation of the company, which is essential; provides for absolute control of the company in the creditors (81.9%) over and against the director-creditors (6%) and the stockholders (12.1%) which is desirable; provides for commencement of operation after the plan in a practically debt-free company which is an economically enviable position; and weighs every phase of the plan in favor of the creditors, which appears to be necessary. While a great deal of criticism of the plan has been done by the Securities and Exchange Commission and despite a two year lapse since the filing of the plan, no one has been able to suggest an alternate plan which has any hope of success. While creditors, including trailer owners have participated in the proceedings, none have seen fit to join the Securities and Exchange Commission in its attempts to dismiss. The proposed plan has a chance of success, a Chapter X would result in ordinary bankruptcy and provide absolutely nothing for any interest. The main point of the Securities and Exchange Commission is that the rights of trailer owners are being affected by the proposed arrangement, which point completely overlooks a unique feature of the plan, i.e. in all particulars where the plan touches the trailer owners, the participation is completely and individually voluntary. No single trailer owner is required (regardless of vote of others) to participate. The

use of the term public-investor creditors in this case is misleading as the claims of trailer owners are based upon unpaid rentals and not upon an unpaid investment debt.

The statute in question, Chapter XI not only does not prohibit the type of arrangement proposed here, but actually anticipates such a use. By allowing adjudgment of all unsecured creditors' rights and by permitting the stockholders to retain rights in the arrangement Chapter XI anticipates the widest possible latitude in the types of arrangement proposed. The Securities and Exchange Commission contends that Chapter XI may not be used where public creditors are involved but if Congress had intended restrictions on the use of Chapter XI when public creditors were involved, the statute would so provide. Far from intending restrictions Congress, by the amendments of 1952 deleting the only restriction in Chapter XI, indicated that set standards were not to be applied to Chapter XI. By the existence of Chapter X and Chapter XI, both directed to adjustment of unsecured debts, Congress intended the use of whichever of the chapters provided the best answer to a particular factual situation. By the reference back and forth between the two chapters, Congress created a counterbalance which operates to the benefit of plans proposed under either chapter.

This Court, in examination of the provisions of Chapter X and Chapter XI has consistently refused to supply restrictions to Chapter XI where none exist. The previous decisions rest on the principle of the lower courts exercising their discretion in determining which chapter best meets the needs to be served. In the case at bar the lower court made an examination and investigation of the plan of arrangement proposed, exercised its discretion and de-

terminated that Chapter X did not best meet the needs to be served. Separating the logic from the irrelevancies, it is clear that the Securities and Exchange Commission wants this Court to declare that the lower courts have no discretion in an arrangement which has public creditors; and wants this Court to declare that the lower court must dismiss such a Chapter XI proceeding. The Securities and Exchange Commission falls far short of establishing reason for this by use of the prior decisions of this Court. Equally as illogical, the Securities and Exchange Commission would have this Court write restrictions into Chapter XI, which restrictions Congress has not seen fit to insert.

The lower courts based their determinations upon the applicable statutes, guided by the prior determinations of this Court as applied to the facts of this case. In so doing, they properly applied the law, followed the precedents and exercised their discretion for the best interest of the creditors of the debtor.

ARGUMENT

THE ARRANGEMENT PLAN, PROPOSES THE SIMPLEST, MOST FEASIBLE AND PROBABLY THE ONLY WORKABLE METHOD OF MEETING THE NEEDS TO BE SERVED.

The plan as confirmed provides that the trailer owners whose trailers are still in the system may exchange their trailers at the rate of one share of stock of Capitol Leasing Corporation for every two dollars of remaining investment; the general creditors at the rate of one share of stock for every \$3.50 of claim; (R. 6) and the stock-

holder claimants, one share of stock for every \$5.50 of claim. (R. 148) As an adjunct to the plan, Capitol Leasing Corporation is purchasing the operating system of American for 107,100 shares of stock. (R. 7) As an overall proposition, no simpler arrangement could be devised as the plan directly attacks every major objection to the previous uneconomic operation of the company, and provides the wherewithall to complete the arrangement.

The Control of Capitol Leasing Corporation Will be in the Trailer Owners

One of the major objections of the operation of the company heretofore has been that the group with the largest financial participation, the trailer owners, have had no way, in law or in fact, to effectively participate in the management of the company.

Under the proposed plan the trailer purchasers will have overwhelming control of Capitol Leasing Corporation.¹ Any management which is selected will be selected at the discretion of this group. This is so because of the weighing of all aspects of the arrangement in favor of the trailer owners. Not only will the trailer owners receive almost three times the amount of stock in Capitol, per dollar, as the stockholder-creditors, but the trailer owners will vote one vote for every share of stock owned and the stockholder-creditors will vote only one vote for every seven shares of stock owned. (R. 148) Stated another way, for every dollar invested, the trailer owners will have two and three-quarter times the ownership and nineteen and one-quarter times the voting power in Capitol Leasing

¹Under the proposed arrangement (presuming 2,000 trailers are delivered to Capitol Leasing) the persons who own stock in Capitol which was received for trailers or claims for trailers will own 79.4% of the outstanding stock of the company.

Corporation as stockholder-creditors. In addition, all of the present stockholders of Capitol Leasing may be classified as trailer owners as they received their stock in exchange for trailers. There is no question but what the trailer owners will exercise complete control of Capitol. The plan also provides that stockholder-creditors will not participate in dividends or liquidation for a period of five years. (R. 148) Of course, management of the two companies is now separate (one common director) but new management beyond this is subject to the complete pleasure of the trailer owners.

The Plan Provides Interim, Experienced Management, Continuous Operation and an Orderly Transition to New Management

While the plan of arrangement itself is the epitome of simplicity, the operation of the system requires experience in the business. The arrangement provides an orderly transition in management and experienced, interested management in the interim. The system, as previously noted, is a network of rental stations. These stations are, for the most part, filling stations located across the United States. (R. 110) Changes in ownership, a lack of business sensitivity and just plain indolence on the part of some of the stations cause recurring problems with which management must deal. The handling of these problems requires knowledge of the books and records of the company, particularly with reference to the original method of setting up stations, to the knowledge of what to do with trailers in a station where that station cancels its contract, to the best manner of handling storage charges where the station attempts to make such charges for periods covered by its contract, to the methods available for tracing missing trailers, to the myriad details in attempting to keep

track of many trailers located all over the United States. For the benefit of trailer owners, the trailer system must be kept in operation and any plan which does not provide for this continuous operation can only result in the probability of total loss to many of the trailer owners.

The trailer owners are not "public investor-creditors" in the accepted sense as they may remove their trailers at any time. The plan, insofar as trailer owners go, is completely voluntary.

The position of the trailer owners should be clearly defined: They were not investor-creditors having only an intangible right or claim against the respondent. They were owners of tangible personal property of which they could take possession. By simple request to the respondent, they could withdraw their trailers from the system and use them elsewhere. (R-157) The respondent, through its records as to the location of the trailers, assisted the owners in finding them. 2600 trailers had been so withdrawn prior to the filing of the Chapter XI petition and an additional 1000 were withdrawn during the course of the proceeding, all with the assistance of the respondent. The trailer was the trailer owner's investment and this could be withdrawn at anytime. The rental claims fall in the nature of general creditors.

Trailer owners were not investor-creditors in the sense used by the Commission as a debenture holder or other unsecured debt security having only an intangible claim for money and at the complete mercy of a debtor for payment or information as to the value of his claim.

The plan of arrangement rejected the leasing agreements by which it operated the trailers as executory con-

tracts and thus voluntarily released the trailers back to the owners. It was expected that the owners of 2000 trailers would elect to leave their trailers in the system and accept the plan. The Commission's phrase "public investor-creditors" is not only not descriptive but is misleading. There could not be any overreaching of the trailer owners by the respondent in the formulation and presentation of the plan to the trailer owners. Each was the master of his own destiny. The acceptance of the plan allowed the respondent to continue to serve the trailers and its efforts to maintain the business.

The directors of American are making continuing contributions of time and money which are more valuable than unneeded machinery of Chapter X.

The proposed plan provides for continued management and at a minimum cost. The directors of the company have assumed the two largest general debts of American and are to receive one share of stock for every \$5.50 of these claims. (R. 149) The directors have also advanced all legal fees and costs involved in the Courts to date, have provided funds for some continuing administrative expense and will have to provide the deposit necessary to final confirmation. In addition, one director has devoted full time to the affairs of the company without compensation. (R. 90) Without these additional contributions of time and money, no program of rehabilitation would be possible. This is coupled with the knowledge of the operation of the system which comes only with experience. The continuation of the knowledge and the continuing contributions by management are a necessary part of most Chapter XI proceedings and are certainly of greater benefit to the trailer owners here than the extra safeguards

of a Chapter X where there has been no showing of the need for the safeguards.² In such a situation, Chapter XI is not only available but is the only workable arrangement.

The plan provides a means whereby non-participating trailer owners may locate and obtain possession of their trailers which might otherwise be lost.

Many of the trailer owners do not desire to participate in the arrangement and are removing or desire to remove their trailers from the system for other purposes. These trailer owners have been, and are being, supplied locations for their trailers and releases authorizing the station operators where the trailers are located to surrender the trailers in his possession to the owners or their agents. In order for this system to continue to function and make the trailers available to the owners, a current location list must be maintained. (R. 112) The cooperation of the station operators must be available. Only in an operating system are these two elements present. The company uses the following method of maintaining trailer location lists. The station operator, using a company form, notifies the company of the departure of a trailer, the destination and other pertinent data; the receiving station,

²As was stated by the court of appeals for the second circuit. In the Matter of Transvision, Inc., 217 F.2d 243.

"The SEC had adduced no information which would tend to indicate that the plan is likely to fail, but has, at most, indicated that there may be some basis for suspecting possible improprieties in past management. Certainly, so ephemeral a suspicion is not an adequate basis upon which to overturn a plan which the District Court, on the facts before it at this time, appears to believe may ultimately be found feasible, and one which, necessarily, would have to be acceptable to at least a majority of the unsecured creditors before being approved. Any dissenting unsecured creditors will be protected if they can show unfair treatment. Mecca Temple, etc. v. Dancock, *supra*. And there is nothing in the action of the District Court which precludes resort by the stockholders or other corporate interests to any other remedies which may be available should any of them seek any redress for any wrongs previously done them by the management."

upon receipt of the trailer, using a company form, advises the company of the trailer arrival; the company uses this information in keeping its own records to date. (R. 111) One miss in reporting by the stations or one miss in recording by the company and the trailer is temporarily lost requiring tracing procedures. Failure of the renter to turn in the trailer or a station refusing to accept a trailer requires immediate administrative procedures. The very philosophy of a Chapter XI requires the company to continue its operations and, in this case, to continue to provide these services. Reference is once again made to the continuing contributions of money and time by the Board of Directors. When filing a Chapter XI, management must be willing to undertake these things and in this case it was done. Neither a Chapter X nor an ordinary bankruptcy can provide these outside contributions. While there are cases where a Chapter X meets the needs to be served, the present case is not one of them.³ It is inconceivable that a Chapter X would work and ordinary bankruptcy would entail a loss, greater even than in the usual bankruptcies.

The assumption that the company can qualify for a Chapter X is fallacious as the leasing agreements would prohibit such qualification.

A Chapter X proceeding would have been doomed to failure from the start. An order transferring to Chapter X would have the trustee take over the operation of the

³The district court, in denying the motion of the Securities and Exchange Commission to dismiss the proceedings, stated at page 145 of the record:

"As I stated at the outset of this hearing, I have studied the file in this case prior to the hearing. I listened to the arguments of counsel, and I am not convinced that the needs to be served here can best be met by a Chapter 10." Later in the same ruling, at page 147 of the record, the district court stated:

"... I think Chapter 11 is available in the state of the matter as it is presented to the Court at this time."

business and take possession of the property and assets of the debtor. The respondent had only office furniture and service equipment. This is all a trustee would have here.

The use of Chapter XI in preference to Chapter X is dictated because the order of transfer and appointment of a trustee, essentially a receiving order, would terminate all leasing agreements concerning the trailers.* Possession would, by operation of such an order, be returned to trailer owners; they would be entitled to all revenue from any subsequent rental of the trailers and not the trustee.

While additional contributions of time and money by the directors, caused by the long delay occasioned by the repeated appeals of the Securities and Exchange Commission, has been a drain on their resources, the real victims of this delay are the trailer owners who wished to participate in the Arrangement. Because of the lapse of time involved, the trailer owners are necessarily confused and uncertain, and in certain instances, unjustified storage charges now constitute liens against the trailers and must now be litigated. It stands to reason that some trailers are lost, damaged and stolen. The dismissal of Chapter XI could result in nothing but frustration of these trailer owners' rights.

An ordinary bankruptcy would mean probable total loss for trailer owners.

If the motion of the Securities and Exchange Commission is granted, the plan is not automatically converted to

*The leases in question provide for automatic termination upon entry of a receiving order. The Referee admitted a lease copy into evidence but it has not been printed as a part of the record.

a Chapter X. If the plan cannot be conformed to a Chapter X, the only alternative is an ordinary bankruptcy.*

Therefore, consideration must be given to the effect of an ordinary bankruptcy.* A trustee would be even less empowered, and inclined, to maintain the locations of trailers.[†] The problems before outlined would be multiplied because the trailers to be removed from the system would include the trailers of the persons who have stated their desire to participate in the plan. While the records turned over to the trustee would be adequate for locations at that time, these records quickly become outdated because of trailer movements. By the time the trailer owners have had an opportunity to evaluate their position and take the necessary steps to obtaining possession, the trailers will, in many instances have moved. Compounding the problems of the trailer owners at this point is the rapidity with which station operators change their operation from trailer rental to trailer storage. Because a Trustee in ordinary

^{*}Annual Reports of the Securities and Exchange Commission. Volumes 25, 26, 27, 28 and 29 show that ordinary bankruptcy is more often the case than conformance to Chapter X. From the period 1959 to 1964, the Securities and Exchange Commission interposed motions to dismiss in 19 Chapter XI cases. 15 of these motions were granted and four denied. Of the 15 granted, eight ended in ordinary bankruptcy and seven were conformed to Chapter X. This is not to say that the eight or some part of them would not have ended as ordinary bankruptcies anyway and this may have been a factor in granting the dismissal. On the other hand, this cannot be taken to say that some may not have succeeded as Chapter XI's. Of interest in this statistic is the noticeable fact that the lower courts are exercising discretion in considering the Securities and Exchange Commission's motions to dismiss and have dismissed (or allowed to be conformed) 15 of the 19. This phenomenal success in persuading the lower courts has not, however, sated the appetite of the Securities and Exchange Commission as they have appealed every case in which they were denied.

[†]The court of appeals stated (R. 161) "The debtor has little or no tangible assets, and if it were liquidated it is not unlikely that the trailer owners, or at least many of them, would have difficulty realizing anything for their trailers."

[†]It is suggested a trustee in an ordinary bankruptcy would be able to do nothing except reject the trailer leases as executory contracts and make the records available to trailer owners for the purpose of determining locations.

bankruptcy would have no interest in the continuation of the rental system, the trailer owners would have to dispute the storage charges, right to possession and even, in many cases, determine the locations of the trailers, as an individual matter. This would create an impossible burden for those who own one trailer (value \$500) facing legal fees, travel and hauling costs, and possible court fees. This does not take into consideration the actions of a few latently dishonest station operators and trailer pirates around the country. The results of lack of an organization in an ordinary bankruptcy would almost certainly be disastrous.

The plan is probably the only plan available to the company, to the best interest of creditors.

To accomplish these highly desirable objectives, the proposed plan has a basic asset which is readily apparent. This asset is the very simplicity of the plan. Capitol Leasing Corporation will commence operation as a going concern with substantially no debts. (R. 5) It will own a fleet of trailers and have a substantial rental outlet system from which to operate the trailers.

But for the intervention of the Commission, the plan would have been completed within a reasonable time after its acceptance on March 7, 1963. Instead, the trailer owners, who are the real parties in interest, have been compelled to stand by and wait and wonder when and how their interests will be settled. Frustration and uncertainty have resulted. Trailers have been lost or stolen. Station operators have, in some cases, gone out of business. Trailers have been lost through foreclosure of storage liens. Trailer owners still hopefully look to Capitol Leasing to continue the business as the only means through which they can now benefit.

At this late date, a transfer of this proceeding to a Chapter X would be futile and fatal; straight bankruptcy would inevitably result. Chapter X would have been futile and fatal a year ago. No interest of secured creditors are involved and Chapter XI seemed then and now the only realistic and proper remedy.

THE STATUTE (CHAPTER XI) DOES NOT PROHIBIT THE ARRANGEMENT PROPOSED BUT RATHER PERMITS AND ANTICIPATES SUCH USAGE. BY USE OF DISCRETION IN THE LOWER COURTS, THE INTERRELATION OF CHAPTER X AND CHAPTER XI CREATES A COUNTERBALANCE TO THE END OF MORE EFFECTIVE USE OF THE TWO CHAPTERS.

The relevant section of Chapter XI provides:

Section 306(1) of Chapter XI (11 U.S.C. 706(1)):

For the purposes of this chapter, unless inconsistent with the context—

(1) "Arrangement" shall mean any plan of a debtor for the settlement, satisfaction, or extension of the time of payment of his unsecured debts, upon any terms;"

As can be seen, nowhere in Chapter XI is the type of arrangement proposed here prohibited. The prohibition exists only in the mind of the Securities and Exchange Commission.

There is no prohibition against this arrangement because such restrictions would require the use of Chapter X as a legalistic exercise in futility.

Is it by the belief that *no* management is capable or desirous of proposing a reasonable arrangement where the public is involved? This question answers itself. Day

by day thousands of people are making determinations and proposals involving the regulation of their transactions with other people in an honest and reasonable manner. This multitude necessarily includes many people involved in management of many business concerns. Certainly we need safeguards against those who do not measure up to this standard of character, and such safeguards are provided in Chapter XI. (In the power of the District Court to dismiss any improper proceeding). It is completely illogical to presume that no management is capable or desirous of proposing a reasonable plan where the public is involved.

What advantages could Chapter X have afforded? A trustee to take over the assets? He could not take over the trailers nor receive any rent from them; nor was there any property of value which he could have realized any upon. Causes of action — against whom and what? The Commission has not said. The necessary expenses of administration which have become traditional in Chapter X, how could they have been paid? In short, the Commission would have a trustee, a complete stranger to the business and to trailer owners, take charge of the business with no assets, taking months to become familiar with the business, and being unable to formulate any plan except one substantially like this and finally being faced with reporting to the Court that he had a plan which might work but unfortunately no money for administration and no trailers left. The legalistic exercise involved in the Section 328 motion seems to intrigue the Commission but would not and has not benefited anyone.

It is quite clear that a receiver would not, in this case, be as capable of operating the business as the man-

agement during the period necessary to effect the plan. This is a service company, its assets are negligible, the fundamental asset (aside from the existence of the system) is the knowledge of the trailer rental business on a nationwide scale, and without this knowledge any operation is foredoomed.

Chapter XI anticipates the exercise of discretion by the courts in a determination as to use of Chapter XI as against Chapter X.

Is this proposal prohibited by the belief that the United States District Courts are incapable of separating the reasonable from unreasonable plans? This is just not true. The very fact that Congress established two methods of reorganizing or arranging with creditors and this Court's reliance on the discretion of the lower courts establishes that the lower courts are capable of making such distinctions, and in fact are required to make such distinctions.* The statute makes only one requirement in a Chapter XI and that requirement is that the arrangement be with unsecured creditors. (Section 306(1), Chapter XI (11 U.S.C. 706 (1)). A Chapter X may deal with secured creditors. Aside from these specific requirements, the

*The comparable provisions of Chapter X and Chapter XI are quite similar (excluding secured creditors) Section 216(1) of Chapter X (11 U.S.C. 616(1)) provides:

"A plan of reorganization under this chapter.—

(1) shall include in respect to creditors generally or some class of them, secured or unsecured, and may include in respect to stockholders generally or some class of them, provisions altering or modifying their rights, either through the issuance of new securities of any character or otherwise;"

Section 306 (1) of Chapter XI (11 U.S.C. 706(1)) provides:

"For the purposes of this chapter, unless inconsistent with the context —

(1) "Arrangement" shall mean any plan of a debtor for the settlement, satisfaction, or extension of the time for payment of his unsecured debts, upon any terms;"

statute makes no distinction and leaves it to the discretion of the Court." It has been argued that this leaves the door wide open for questionable tactics by management, but this is not true. The relative informality of a Chapter XI is controlled by the discretion of the lower court to dismiss, if a plan is proposed which requires the formal procedure of a Chapter X. This determination must be based upon the meeting of the needs to be served, not upon an arbitrary determination that certain types of creditors (except secured) have claims against the company. (*General Stores Corp. v. Shlensky*, 350 U.S. 462). The Securities and Exchange Commission completely overlooks the fact that such distinctions could have been included in Chapter XI if Congress had so intended. This Court has stated that such distinctions do not exist and the general determination must be based upon the needs to be served. (*General Stores Corp. v. Shlensky, supra.*)

Chapter X is not the panacea of distressed Corporations the Securities and Exchange Commission would have us believe it is.

As opposed to the acceptance of the plan proposed by the respondent in three months, the district court observed that Chapter X reorganizations are expensive, time consuming and didn't work. (R-144) The district court was justified in its conclusions.

*A clear statement of this principle is set forth in the Matter of *Transvision, Inc.*, 217 F.2d 243, 246 Writ of Certiorari denied 75 S.Ct., 440.

"The Supreme Court has declared that this determination as to the adequacy of the relief afforded by Chapter XI is one within the purview of the district court's discretionary exercise of its equity powers, *Securities and Exchange Commission v. U.S. Realty Co., supra*, 310 U.S. at page 450, 60 S.Ct. 1044, and unless the petitioner's corporate and financial condition is demonstrably such as to indicate that the district court has abused that discretion, its determination should be sustained."

The 25th through 29th annual reports of the Commission for its fiscal years ended June 30 of 1959 through 1963 illustrate the length of time involved in corporate reorganization and the probability of success. The cases named in these reports do not purport to be all of the corporate reorganization cases in that the Commission selected those in which it participated. These cases (parent and subsidiary are regarded as one case) are summarized:

	1959	'60	'61	'62	'63
Number of cases in which					
Commission participated	49	52	56	64	91
New cases during year	14	9	11	18	32
Cases closed during year	4	7	8	5	13
Cases remaining at end of year in					
which Commission was participating	45	45	48	59	78

These reports merely refer to the cases as "closed" which may mean the Commission withdrew from participation, the debtor was thrown into straight bankruptcy, or that there was a reorganization. Only one case (Muntz T. V. Inc.) might be regarded as a completed reorganization. While the Commission does not control the full course of reorganization and each case must stand on its own facts, the above summaries do illustrate the time and uncertainties involved in reorganization. They also cast some doubt on the Commission's "expertise" in the area of corporate reorganization.

These reports also refer the Chapter X cases initiated in the district court for Colorado and show their termination, three in straight bankruptcy. Another (U. S. Durox of Colorado) is described as a reorganization by

liquidation of assets which was actually a sale of all of the assets of that debtor to the holder of the mortgage on all its assets; the holder of the mortgage (Small Business Administration) was allowed to foreclose, but required to pay the expense of administration of \$121,000 and creditors got nothing.

Again an examination of these annual reports of the Commission illuminate the accomplishments of the trustee. Of the cases referred to in these annual reports; only two are cited which show the recovery of money by a trustee.

The Securities and Exchange Commission must prove that a Chapter X is available to the particular debtor as a part of its motion to dismiss under Section 328 which it has not done.

The Securities and Exchange Commission has overlooked a relevant portion of the very section upon which this matter rises. Section 328 provides:

• Chapter XI, Bankruptcy Act; Section 328 (11 U.S.C. §728)

"Dismissal Proceedings; Amended Petitions"

"The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings *should have been brought* under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirements of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition

under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title be deemed to have been originally filed under such chapter." (Emphasis added)

The portion overlooked by the Securities and Exchange Commission in all of its arguments is that the plan may be dismissed if the judge finds the proceedings should have been brought under chapter 10. The language of the statute limits the application of the section to a case which should have been brought under Chapter X, a fortiori, can qualify under Chapter X. To date the Securities and Exchange Commission has conveniently ignored this portion of the section and has not presented any evidence to indicate the availability of Chapter X¹⁰ and it is clear that Chapter X is not available.

There is no proof of need for a Chapter X.

However, presuming, arguendo, that the Securities and Exchange Commission had proved the availability of Chapter X and even that the proceedings should have been brought as a Chapter X, the court is still not required to

¹⁰The Securities and Exchange Commission must establish its contentions by factual presentation as is set forth in *Grayson-Robinson Stores, Inc. v. Securities and Exchange Commission*, Second Circuit, 32 F.2d, 940, 949.

"The Commission (Securities and Exchange Commission) is no more relieved from the need of producing evidence on such a factual issue than are other litigants; . . . The Securities and Exchange Commission, in the case at bar, did not present evidence on most of its allegations, relying instead on innuendo and implication. No good reason appears at hand for this failure, particularly when granting of the motion to dismiss would harm the very persons (the trailer owners) who the Securities and Exchange Commission claims to be protecting.

dismiss as the responsibility for determining the appropriateness of a particular plan rests ultimately with the district court. At no point has the Securities and Exchange Commission indicated the need for a Chapter X except that they would like to run an investigation. The company has filed a full disclosure registration with the Securities and Exchange Commission and the prospectus is a part of the record here, and had, prior thereto undergone investigation by the Securities and Exchange Commission, and yet nothing was acquired from these investigations of relevance to this proceeding. The Securities and Exchange Commission did not show the court any irregularities of management for which corrective action could be taken.¹¹ The purpose of an arrangement is not the pursuit of a will-o'-the-wisp but to see that the needs to be served are met. This is particularly true where the instigator of the pursuit can advise the court of no purpose in the pursuit. The Securities and Exchange Commission would superimpose upon Chapter XI a ~~new~~ section, absolutely excluding from its operation a plan which provides for public investor-creditors with participation by stockholders. The statute clearly does not so provide¹² and if Congress had so

¹¹One of the original directors appropriated about \$140,000 of the funds of the company. That director died, leaving no estate. This amount was intended for trailer purchase and the subject trailers were subsequently manufactured and paid for.

¹²In fact the statute provides quite the contrary;

Chapter XI, Section 366 (11 U.S.C. §766)

* "Requisites for confirmation

"The court shall confirm an arrangement if satisfied the — (1) the provisions of this chapter have been complied with; (2) it is for the best interests of creditors and is feasible; (3) the debtor has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of a bankrupt; and (4) the proposal and its acceptance are in good faith and have not been made or procured by any means, promises or acts forbidden by this title.

"Confirmation of an arrangement shall not be refused solely because the interest of a debtor, or if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement."

In the case at bar the stockholders have, in fact, retained a minor (12%) interest in Capitol Leasing Corporation.

intended the statute would so provide. If the Securities and Exchange Commission is sincerely convinced that the district courts, as a whole, are incapable of exercising the discretion which the statute and this Court provide, let them approach Congress, advise them of the ineptitude of our judiciary, and have the statute amended.

Chapter X and Chapter XI both provide for arrangements with unsecured creditors and thereby provide a counterbalance, one for the other.

The statutes which are presently in effect and not those which the Securities and Exchange Commission would like, are those with which we must deal. In the relevant portions, Chapter X and Chapter XI are similar. That is, they both are intended for the arrangement of unsecured creditors' claims and continuance of operation of the company. The rationale of the existence of the two means of alleviating the financial stress of a corporation becomes readily apparent when one considers the portion of each statute in which reference is made to the other statute. Chapter X provides that it must be shown that Chapter XI does not provide adequate relief.¹³ Chapter XI provides that it may be dismissed if the proceeding should have been brought under Chapter X.¹⁴ The obvious intent

¹³The relevant section provides:

Chapter X, Section 130 (11 U.S.C. §530)

"Every petition shall state — (7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter 11 of this title; . . ."

¹⁴Chapter XI, Section 328 (11 U.S.C. §728) which is set forth in full at page 3 hereof provides generally that the judge may, if he finds the proceedings should have been brought under Chapter X, enter an order dismissing the proceedings unless the petition is amended to conform to Chapter X.

is that use of Chapter XI is preferred,¹⁵ but the foregoing provision of Chapter XI operates as a counterbalance, for if the court finds the arrangement needs the safeguards of Chapter X, it may dismiss. No such need has been shown here. Conversely, a proceeding under Chapter X may be transferred to a Chapter XI if Chapter XI would provide adequate relief.¹⁶

The district court correctly applied the provisions of Chapter XI to the case at bar.

A question to be asked at this point is, did the district court follow the apparent dictates of the statute? The court (in the person of the Senior Referee in Bankruptcy as Special Master) investigated the potential of recovery of monies from past management. He was advised that there was no possibility of recovery of any monies from past management and present management could completely account for their stewardship. (R. 122-125) The Securities and Exchange Commission offered nothing contrary to this position, despite their previous investigation, and this stands uncontradicted. The court (in the person of the Senior Judge of the District, Alfred A. Arraj) pro-

¹⁵As stated by the court of appeals, second circuit, *In the Matter of Transvision, Inc.*, 217 F.2d 243.

"Indeed, the Bankruptcy Act itself, in requiring every petition under Chapter X to state 'why adequate relief cannot be obtained under Chapter XI' Bankruptcy Act, §130(7), 11 U.S.C.A. §53(7), and in declaring that 'A (Chapter X) petition shall be deemed not to be filed in good faith if*** (2) adequate relief would be obtainable by a debtor's petition under the provisions of Chapter 11 of this title,' Bankruptcy Act §146, 11 U.S.C.A. §546, manifests a conscious purpose of Congress to encourage resort to Chapter XI whenever the remedy afforded thereby adequately protects the interests involved."

¹⁶The relevant section provides:

Chapter X, Section 147 (11 U.S.C. §547)

"Amendment of Petition to Comply with Provisions Governing Arrangements

"A petition filed under this chapter improperly because adequate relief can be obtained by the debtor under chapter 11 of this title may, upon the application of the debtor, be amended to comply with the requirements of chapter 11 for the filing of a debtor's petition, and shall thereafter for the purposes of chapter 11 be deemed to have been originally filed thereunder."

pounded objections to the plan of arrangement. (R. 146) Each of the objections resulted in direct action in the form of an amendment to the plan. (R. 148-150) It was clear that if the plan, in its final form, was not what the court considered proper, it would be dismissed. (R. 146) The Securities and Exchange Commission has not renewed its motion to dismiss but has appealed on the single point that the proposed plan adjusts the rights of the trailer owners and provides some participation to the stockholders. An examination of the plan shows a drastic reduction from the previous position occupied by the stockholders of American in addition to the continuing contributions of the directors. (R. 7)

The proper application of the provisions of Chapter XI has afforded the company a chance for success to the benefit of the interests to be served.

The proposed plan is not prohibited by the statute. To the contrary, the logic of the statute anticipates the handling of a plan of arrangement in the manner this matter was handled. The statute is focused on the duty of the district court.¹⁷ If the plan is one which is shown to require the use of the cumbersome machinery of Chapter X, dismiss the Chapter XI. If the plan is one which is proper as proposed or as amended, use the more economical route of Chapter XI. Thus the two chapters act as counterbalances for each other. They prevent oppressive or unfair plans on the one hand, and allow proper plans to function without oppressive machinery on the other. By proper exercise of its discretion, the district court can effect a real service to the interests to be served in a distressed corporation. The district courts have this dis-

¹⁷In the case of an improper Chapter X, the court may permit amendment to Chapter XI; in case the Chapter XI proceedings should have been brought as a Chapter X, it may dismiss; which actions are within the sound discretion of the district court.

cretion (*General Stores Corp. v. Shlensky*, 350 U.S. 462) and the exercise of discretion is the bulwark of any effective plan. To wed a corporation to a Chapter X merely because of the existence of a particular type of creditor is to leave many corporations with no alternative to ordinary bankruptcy. Clearly, the statute does not anticipate this, but intends that a corporation with a fair opportunity for success have that opportunity.

THE LOWER COURTS, IN EXAMINING A PROPOSED CHAPTER XI, ARE BOUND TO EXERCISE A SOUND JUDICIAL DISCRETION IN DETERMINING WHETHER A CHAPTER XI MEETS THE NEEDS TO BE SERVED AND ARE BOUND BY ARBITRARY STANDARDS. IN THIS CASE THE COURT CORRECTLY DETERMINED THAT CHAPTER XI MET THOSE NEEDS AND CHAPTER X DID NOT.

This Court has long recognized the necessity of flexibility in application of Chapter X or Chapter XI, which recognition is most evident in the application of the doctrine of "discretion of the lower courts."¹¹ The previous decisions on the question have indicated the awareness of this Court that no set formula can be applied in every case.¹² They recognize that in two given cases, with similar

¹¹*General Stores Corp. v. Shlensky*, 350 U.S. 462-468:

"We could reverse their (the lower courts) only if their exercise of discretion transcended the allowable bonds."

¹²*General Stores Corp. v. Shlensky*, 350 U.S. 462, 465:

"Much of the argument has been devoted to the meaning of Securities & Exchange Com. v. United States Realty & Improv. Co. 310 U.S. 434, 84 L.ed. 1293, 60 S.Ct. 1044. In that case we held that relief was not properly sought under Chapter XI but that Chapter X offered the appropriate relief. That was a case of a debtor with publicly owned debentures, publicly owned mortgage certificates, and publicly owned stock. An arrangement was proposed that would leave the debentures and stock unaffected and extend the certificates, and reduce the interest. It was argued that in that case, as it has been in the instant one, that Chapter X affords the relief for corporations whose securities are publicly owned, while Chapter XI is available to debtors whose stock is closely held; that Chapter X is designed for the large corporations, Chapter XI for the smaller ones; that it is the character of the debtor that determines whether Chapter

capital structure and similar creditors, one may require a Chapter X and the other may best function under a Chapter XI. In its reasoning, this Court has followed the dictates of the provisions of the state and has refused to sanction the application of arbitrary standards. (*General Stores Corp. v. Shlensky*, 350 U.S. 462, 465). This Court has rather, directed the lower courts to exercise discretion in determining whether a Chapter X or a Chapter XI is the proper forum. The lower courts having heard the witnesses, met with creditors, examined the plan and watching the administration in general, is the proper body to exercise discretion. The lower court may be reversed if it has clearly abused its discretion. (*General Stores Corp. v. Shlensky, supra.*) But in this case, the question presented is not abuse of discretion. The question challenges the judgment of the lower court and states that the arrangement proposed cannot be done under Chapter XI. This challenge does not stand to the test of reason, to the test of an examination of the statutes involved, or to the test of previous decisions.

This Court has previously rejected the imposition of arbitrary standards, relying instead on the discretion of the lower court and in this case, the lower court, in the exercise of that discretion, committed no abuse.

The Securities and Exchange Commission has previously contended that particular capital structure or the presence of particular types of creditors determines with finality the propriety of Chapter X or Chapter XI. This proposition has been firmly rejected by this Court. (*General Stores Corp. v. Shlensky*, 350 U.S. 462) In the course of rejecting that contention, this Court has advised that reversal may be had only upon an abuse of discretion by

¹⁸ (continued)

X or Chapter XI affords the appropriate remedy. We did not adopt that distinction in the **United States Realty** case."

the lower courts. (*General Stores Corp. v. Shlensky, supra.*) This is clearly the tenor of the statutes themselves. Yet the question is not based upon an abuse of discretion. The reason for this is clear enough; there was no abuse of discretion. The lower court examined the plan, the history of the company, heard the statements of counsel, heard the participating creditors, examined witnesses, and made some objections to the plan; (R. 146).

"Now, I have, or, I want to express for the record some objection to the proposed plan. I do not think that the proposed plan gives the owners of the trailers a fair shake.

"In other words, unless this plan that is finally determined in this case under the Chapter 11 is such a plan that the investors themselves will have control of this corporation and not the management who got it in this shape, then I say it will be an improper plan. Therefore, that would suggest that the investors should have more than one share of stock for each two dollars and management less than one share for each three dollars and a half, but at any rate, the proportion of the ratio should be such as the investors will have control of the corporation. This is the only way, in my opinion, that it can properly operate.

"Now, also in connection with the plan, consideration should be given to treating all creditors alike. One creditor should not be paid just because the officer guaranteed that payment and another creditor not paid in cash. The bank, for example. These people are knowledgeable in this business. They are sophisticated lenders, and to treat them with some special treatment as against an individual who is a creditor is not, in my opinion, equity or justice."

An examination of the amendments thereafter made (R. 148-150) indicates the firmness with which the district court handled this arrangement. Given the opportunity which Chapter XI affords, the court can, and under a proper exercise of its discretion will, perform a valuable service in this area. This service many times includes, as in this case, the opportunity for creditors to considerably improve their position over that which they would occupy in an ordinary bankruptcy as the only other available procedure. (R. 161)

If restrictions such as requested by the Securities and Exchange Commission had been intended to be applied to Chapter XI, Congress would have so provided.

Had Congress intended to restrict the use of Chapter XI to only certain types of creditors, or intended to exclude certain types of creditors, such a restriction or exclusion could have easily been included in the statute. But no such restriction or exclusion exists. This Court has twice refused to assume the responsibility of the legislative branch and has not itself written such restrictions where none exist. (*General Stores Corp. v. Shlensky*, 350 U.S. 462) (*Securities and Exchange Commission v. United States Realty & Improvement Co.*, 60 S. Ct. 1044).

The Securities and Exchange Commission wants the absolute priority of claims doctrine applied even though it has been removed from the statute and Congress has made clear that it is not to be applied.

The main burden of the Commission's brief is that a plan of arrangement under Chapter XI should be judged by Chapter X and that the "fair and equitable" standard and the rule of absolute priorities of Chapter X must be

applied in determining whether a Chapter XI proceeding should be transferred to Chapter X and further that any preservation of interests of stockholders without new contributions on their part violates this standard and rule.

This argument fails to recognize the full import of the 1952 amendments to Chapter XI and the Congressional purpose and intent in amending the Chapter. The amendment to Section 366 (11 U.S.C. §766) of Chapter XI eliminated this standard and rule from consideration. The section now provides that the plan be "feasible" and "in the best interest of the creditors", and appears as follows:

"Requisites for Confirmation

"The Court shall confirm an arrangement if satisfied that — (1) the provisions of this chapter have been complied with; (2) it is for the best interests of the creditors and is feasible; (3) the debtor has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of a bankrupt; and (4) the proposal and its acceptances are in good faith and have not been made or procured by any means, promises or acts forbidden by this title."

Another paragraph was added to the section at that time which clearly established the intention of Congress. Section 366 (11 U.S.C. §766)

"Confirmation of an arrangement shall not be refused solely because the interest of a debtor, or if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement."

The Securities and Exchange Commission will have us believe that this amendment was "perfecting or clarifying". However, the legislative history of the amendments does not substantiate this view, and quite the contrary, shows that the changes were substantive: U.S. Code Cong. & Admin. News, 1952, P.1981, 1982, 82nd Cong. 2d Sess., p. 21, H. R. Rep. No. 2320:

This amendment to Section 366 gives further meaning to Section 306(1) (11 U.S.C. 706(1)) that an "arrangement may mean any plan — for the settlement, satisfaction — of unsecured debts, *upon any terms*" and Section 357(8) (11 U.S.C.) that an arrangement may include "any other appropriate provisions not inconsistent with this Chapter. Since Section 366 allows preservation of interests of stockholders without new contributions from them, a plan which preserves the interests of stockholders to some extent only and which gives preponderant and dominant control to creditors is not inconsistent with Chapter XI.

Congress made a clear and definitive statement as to its purpose and intent in eliminating "fair" and "equitable" and the rule of absolute priorities from consideration in Chapter XI. This is explained in Senate Report No. 1395, 82d Cong., 2d Sess. (1952):

"Sections 35, 43, and 50 of the bill make similar changes in section 366 (3), 472 (3), and 656a (3) of the act. The language 'fair and equitable' was derived from section 221 (2) of Chapter X, in which, for the purposes of a corporate reorganization, the requirement is sound and necessary. However, the fair and

equitable rule cannot be applied in a Chapter XI, XII, or XIII proceeding, if construed as interpreted in *Northern Pacific Railway Co. v. Boyd* (228 U.S. 482, 33 S.Ct. 554, 57 L.Ed. 931 (1913), and reaffirmed in *Case v. Los Angeles Lumber Products Co., Ltd.* (308 U.S. 106, 41 Am. B. R. (N. S.) 110, 60 S.Ct. 1, 84 L.Ed. 110 (1939)), without impairing, if not entirely making valueless, the relief provided by these chapters. If so applied, no individual debtor or corporate debtor (where stock ownership is substantially identical with management) under chapter XI, and no individual debtor under chapter XII or XIII can effectuate an arrangement or plan by scaling of debts.

"The fair and equitable rule was never applied in a composition proceeding under the former section 12 of the Bankruptcy Act, which has been replaced by Chapter XI, nor is it practicable or realistic to apply it in a proceeding under Chapter XI, XII, or XIII.

"The amendment removes the 'fair and equitable' provision and by a paragraph added to each of the amended sections it is made clear that it shall not be applied thereunder.

To the same effect, is the House Report No. 2320, 82nd Cong., 2d Sess. (1952) 21.

The amendment does not mean that a plan can be unfair (in the general sense of the word) it merely signifies the recognition of the unworkability of the absolute priority rule in certain cases. As a prime example, the present case. The trailers must be kept in operation through continuous administration of the company; the company is, in ef-

fect a service company providing a rental outlet for the many trailers owned by individuals; the leases for the operation of the trailers are uneconomical; any arrangement providing cash payment of the back obligations to trailer owners is unrealistic in view of the continuingly increasing obligations on current operation of the trailers; therefore, the ownership of the trailers must be in the company; the most economical manner of obtaining a system is one where the previous owners of that system delay their compensation until such time as the system is paying its way, hence the issuance of stock for the system as an incident of the plan. The issuance of shares of Capitol Leasing Corporation to the shareholders of the respondent for the assignment of the rental system gave meaning to the plan; it did not adversely affect creditors or trailer owners to have this stockholder interest continued. Since respondent had no significant assets, creditors would have received nothing in bankruptcy or Chapter X. The method proposed provides an operating system and the trailers to operate, both in a substantially debt-free company. While it would be difficult to say that Congress specifically had this particular case in mind when amending Chapter XI, it is not beyond the realm of reasonableness to say that Congress generally had such a situation in mind.

That Congress did not have in mind the restrictions which the Securities and Exchange Commission would impose is clear from the statute itself. At no place in Chapter XI is such a restriction mentioned. This Court has, when asked to write this type of restriction, twice refused. (*General Stores Corp. v. Shlensky*, 350 U.S. 462) (*Securities and Exchange Commission v. United States Realty & Improvement Co.*, 60 S.Ct. 1044). This Court has, to the contrary, said that no such restrictions exist and that the

only grounds for appeal is abuse of discretion by the lower court. This case does not involve an abuse of discretion but rather involves an attempt by the Securities and Exchange Commission to have this Court reimpose the doctrine of absolute priority in a statute from which Congress has previously removed it.

The lower courts have a maximum control over the reasonableness or general fairness of a Chapter XI proceeding.

Of course, this does not give license to the imposition of an unreasonable or improper plan upon creditors, even after confirmation, because of the counterbalance provided by the interrelation of Chapter X and Chapter XI. If the plan proposed under Chapter XI is improper, the lower court may dismiss it. If the company is the type which can seek relief under a Chapter XI, a Chapter X can be transferred. This is possible by the provisions of Section 328, Chapter XI, *supra*. This section, in relation to Chapter X, Sections 130 and 147, *supra*, can lead to only one conclusion. A wide latitude of arrangements are possible under a Chapter XI which must operate only at the discretion of the district court. This has been the tenor of the opinions of this Court. By these precepts the statutes provide the greatest possible assistance to rehabilitation of financially distressed companies and the salvation of creditors' interests.

The lower court, in this case, exercised its discretion after an examination of all factors, followed the dictates of the statute and this Court and provided an opportunity for meeting the needs to be served which is vastly superior to the only alternative, ordinary bankruptcy.

Has the lower court exercised its discretion in this matter? The answer is a clear yes. The district court made clear that it felt that the trailer owners were entitled to more stock in ratio to the director-stockholder creditors. (R. 146) The plan was amended (prior ratio 4 to 7 pro rata on dollar amounts claimed, in favor of trailer owners, amended ratio 4 to 11 in favor of trailer owners). (R. 148-150) The court felt two creditors were being favored. (R. 146) The plan was amended. (These obligations were assumed by some of the directors and stock will be issued at the same 4 to 11 ratio in favor of the trailer owners) (R. 149) The court wanted control of the new company in the trailer owners. (R. 148) The plan was amended (the director-creditors voting only one vote for every seven shares of stock, — voting ratio 4 to 77 pro rata on dollar amounts claimed in favor of the trailer owners — the director-creditors not participating in dividends or liquidation for five years). (R. 148-149) The court had closely examined the plan and, exercising its discretion, stated its position in this matter. That the debtor had already determined on amendments is not significant. The point is that the court has examined the plan and determined it wanted changes. The lower court followed the logic of the statute and the dictates of this Court. By prudent exercise of the court's discretion, this corporation has been given the opportunity to salvage some of the interests of the concerned parties. This is to be contrasted with the only other alternative, ordinary bankruptcy. (R. 161)

CONCLUSION

On December 20, 1962, when the petition was filed in this proceeding, American Trailer Rentals Company was a company with no substantial assets. It was obligated on leases which were useless to the trailer owners and an impossible burden on the company. Its obligations were mounting daily and it was readily apparent that no solution existed for the company within the framework of the contractual obligations which it faced. Of necessity it had to seek relief under such statutes as might afford it relief.

The only alternatives available to this company were: (1) Ordinary Bankruptcy — which provided nothing for the trailer owners, the general creditors or the stockholders; (2) Chapter XI — which provided a relatively simple manner of adjusting the claims of creditors, including trailer owners; the continuance of experienced management and maintenance of the system, primarily for the benefit of trailer owners. It presented a choice to the trailer owners to remove their trailers or leave them in the system, voluntarily; and (3) Chapter X — by virtue of which a trustee would be appointed and a lengthy time allotted to examination of the affairs of the company. He must report to the creditors on his findings and devise a plan. He must thereafter submit the plan to the Securities and Exchange Commission and to the court. Then and only then may the plan be submitted to the creditors to determine if it is acceptable. Any feasible plan, when and if evolved, would necessarily be based upon the same structure as the plan herein proposed. This procedure would more likely end in the trustee reporting that because of the lack of funds and the time consummed, no feasible plan under Chapter X could be presented. It is evident

the only result would be ordinary bankruptcy with no assets to distribute to creditors and with many trailer owners' trailers becoming lost. Any attempt now to convert to Chapter X at this date would result in a greater loss to the trailer owners.

The plan proposed, accepted by the creditors, including trailer owners, approved and confirmed by three separate courts, provides a fair arrangement with the trailer owners for their trailers, and provides the only feasible manner of meeting the needs to be served of the interests involved. In refusing to dismiss, the lower courts properly exercised their discretion and allowed the trailer owners, whose interests are paramount, an opportunity to salvage something from their trailers which neither ordinary bankruptcy nor Chapter X could provide.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1964

No. 35

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

AMERICAN TRAILER RENTALS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF
APPEALS FOR THE TENTH CIRCUIT

**REPLY BRIEF FOR THE SECURITIES AND EXCHANGE
COMMISSION**

**1. A CHAPTER XI ARRANGEMENT IS NOT THE ONLY
FEASIBLE METHOD OF REHABILITATING THE DEBTOR'S
BUSINESS**

Throughout the respondent's brief (pp. 9, 17, 18, 19, 20, 21, 22, 24, 25) runs the contention that its business can survive only through the proposed Chapter XI arrangement and that the grant of the Commission's motion would lead to total collapse of the enterprise with attendant losses to all interests. Such a contention has been made in virtually every Chapter XI proceeding which the Commission has sought to

transfer to Chapter X.¹ An adjudication in bankruptcy is, of course, always possible when a debtor seeks relief under one of the rehabilitation procedures of the Bankruptcy Act, but adjudications in bankruptcy have occurred more often after denial of a motion by the Commission under Section 328 than after the grant of such a motion.²

Moreover, further financial difficulties are more likely after a Chapter XI proceeding than after a Chapter X proceeding—presumably because the latter

¹ For example, in *General Stores Corp. v. Shlensky*, 350 U.S. 462, the debtor's president submitted an affidavit that proceedings under Chapter X would endanger the debtor's interests in its only assets, two wholly-owned subsidiaries whose stock the debtor had pledged (Record, No. 170, O.T. 1955, 45a-46a).

² From July 1, 1953, to date there have been fourteen proceedings in which motions of the Commission under Section 328 of the Bankruptcy Act have been granted. Six of the debtors involved were subsequently reorganized under Chapter X, five Chapter X proceedings are pending, and only three of the debtors were adjudicated bankrupt. During the same period there were ten Chapter XI proceedings in which the Commission's motions to dismiss were denied, and of these only two of the debtors have consummated an arrangement, three proceedings are pending and five have been adjudicated bankrupt. See Appendix A, *infra*, p. 10.

Respondent states (Br. 19, fn. 5), without explicit citation, that Volumes 25-29 inclusive of the Commission's Annual Reports show that the Commission made motions to dismiss in nineteen Chapter XI cases, of which fifteen were granted, and that of these "eight ended in ordinary bankruptcy." These reports do show that during the years they cover (fiscal 1959 through fiscal 1963) nineteen such motions were made by the Commission, but, as shown by Appendix A, *infra*, only eight of the motions were granted, and not eight—but only three of the corporations involved in these eight cases were adjudicated bankrupt.

permits a far more thoroughgoing reorganization than the former. The Commission's experience has been that bankruptcy proceedings rarely occur after a Chapter X plan has been consummated, and it is common knowledge that companies which undergo a readjustment of their unsecured debts under Chapter XI not infrequently find it necessary to make another trip to the bankruptcy court. This Court has warned that unless there has been the complete inquiry into a company's affairs and prospects which Chapter X contemplates, the debtor's "revived financial life" after a Chapter XI proceeding might be "too short to serve any public or private interest other than that of [the company]" (see *Securities and Exchange Commission v. United States Realty & Improvement Co.*, 310 U.S. 434, 456; and that "[w]ithout a new management today's readjustment [under Chapter XI] may be a temporary moratorium before a major collapse" (*General Stores Corp. v. Shlensky*, 350 U.S. 462, 466).

The various advantages of the proposed Chapter XI plan to which respondent refers (Br. 11-17, 38-39) would also be available under Chapter X. A plan under Chapter X could provide for: a new corporation; the transfer of the trailer rental system to it; the conversion of public investor-creditors into stockholders; settlement of the claims of other creditors; new management (which might well be necessary); and a trustee who could maintain interim operation of the system, could employ present management to

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assist him,⁴ and, if appropriate, could provide trailer location information to investor-creditors wishing to withdraw their trailers.⁵

The statement that "the order of transfer and appointment of a trustee, essentially a receiving order, would terminate all leasing agreements concerning the trailers" because "[t]he leases in question provide for automatic termination upon entry of a receiving order" (Br. 17-18) is not supported by the record. The only trailer lease admitted into evidence (Commission Exhibit E, Tr. 590-591) was described as "typical" of the "greater majority" of the debtor's leases (R. 104). It provides that the term of the lease is ten years and it contains no provisions for termination prior to the end of the term, except if the trailer is destroyed or stolen. (The lease is not a part of the printed record; it is reprinted in Appendix B, *infra*, pp. 12-15.)

Moreover, the record does not support respondent's claim (Br. 11) that the proposed plan provides a "workable method of meeting the needs to be served."

⁴ While the debtor's peak monthly income of \$60,000 had diminished to \$14,000 by the time the Chapter XI petition was filed, and as a result of trailer withdrawals has necessarily diminished further since then, the record indicates that the debtor continues to have income from trailer rentals (R. 93). Such income was approximately \$4,000 per month when the Commission filed its motion to transfer (Tr. 292), and was expected to increase (R. 113).

⁵ The record does not support the claim that ordinary bankruptcy would mean probable total loss for public investor-creditors (Br. 18-20). No reason appears why a trustee in bankruptcy could not maintain trailer location records or why the receipt of trailers by public investor-creditors would entail any more loss to them than has been incurred by those who have already withdrawn a total of about 3600 trailers (Br. 14).

Although the debtor believed that it would need many thousands of trailers to operate profitably (R. 76, 115-116, 127), the reorganized company would have only a relatively small number of them available after the arrangement.* Indeed, it cannot even count on all the trailers that are now in the system, since dissenting trailer owners cannot be forced to transfer their trailers to the new company. See Section 367(1) of the Bankruptcy Act, 11 U.S.C. 767(1). Furthermore, the record does not show that the reorganized company could obtain the capital necessary both for purchasing the additional trailers (apparently needed for profitable operation) and for other purposes (R. 157, Br. 15). In short, "this business needed a more pervasive reorganization than is available under c. XI" (*General Stores Corp. v. Shlensky*, 350 U.S. 462, 468).

2. CHAPTER XI DOES NOT PROVIDE ADEQUATE PROTECTION FOR PUBLIC INVESTOR-CREDITORS WHOSE RIGHTS ARE TO BE READJUSTED

In our main brief we urged (pp. 22-39) that public investor-creditors require the protection which Congress provided in Chapter X for investors in corporations undergoing reorganization, and pointed out several reasons why such protection is particularly needed in the present case. The *amici curiae* (who are parties to the *Securities and Exchange Commission v. Burton* case, No. 6623, which is now pending before the Court of Appeals for the First Circuit on the Commission's appeal from an order refusing to transfer a Chapter XI proceeding to Chapter X)

* The debtor estimated that 2000 trailers would be surrendered under the proposed plan (Br. 7-8). In addition, Capitol owns 299 trailers (R. 5).

urge (Br. 19) that this Court's decision should not go beyond the particular facts involved in the present case. They state (Br. 20-21, 25-26) that in the *Burton* case procedures have been provided in the Chapter XI proceeding that give substantially the same protection to public investors that Congress provided in Chapter X, and that in a Chapter XI proceeding the Commission "as an intervenor, can participate in the necessary determination by the referee and the court just as effectively as in a Chapter X proceeding * * *."

Of course, the Court decides only the particular case before it. In deciding this case, however, we think it would be appropriate for the Court to announce, as a governing principle, that transfer to Chapter X is required whenever the rights of public investor-creditors will be adjusted in the reorganization.* We have set forth in our main brief the reasons why we believe that this principle is sound. We urge this Court, if it agrees with us, to announce the principle because, in this area of the law, it is desirable for the lower courts to have the clearest possible guidelines in order to minimize litigation which not only burdens the Commission and the lower courts, but also delays necessary financial rehabilitations of distressed corporations.

In any event, the *amici's* argument rests upon misconceptions as to both the scope of the Commission's

* But cf. *Securities and Exchange Commission v. Crompton Builders, Inc.* (C.A. 5, No. 20712, decided October 21, 1964), where the court, in reversing a district court's refusal to transfer a Chapter XI proceeding to Chapter X, seemingly refused to adopt any broad principles and held only that, on the facts of the particular case, "the district court went beyond sound judicial discretion" (slip op., p. 14) in denying a transfer.

participation in a Chapter XI proceeding and the extent of the protection which the latter may provide for public investor-creditors. Chapter XI does not authorize the Commission to participate, except to the limited extent of filing a motion under Section 328 to transfer the proceeding to Chapter X.⁷ If the district court denies such a motion, the Commission's powers and interest in the proceeding are at an end. Furthermore, even if the district court should provide some provisions specially designed to protect the public investor-creditors (such as the appointment of a receiver, which occurred in the *Burton* case), this would still fall far short of affording these investors the full measure of the protection which only Chapter X can, and does, provide. See *Securities and Exchange Commission v. United States Realty & Improvement Co.*, 310 U.S. 434, 449-451. Furthermore, since the motion to transfer normally is made early in the Chapter XI proceedings (in order to avoid delay), it is usually impossible to know at that time what additional protections, if any, the court may see fit to impose after all the pertinent facts have been developed in the course of such proceedings.

⁷ The *amici* point (Br. 12) to the Commission's attempted intervention in this case in order to oppose the confirmation of the plan. As explained in our main brief (p. 14, fn. 12), the Commission sought to intervene in its capacity as administrator of the Securities Act of 1933, in order to prevent a distribution of securities under the plan which it believed would violate the antifraud provisions of that Act (Section 17(a), 15 U.S.C. 77q(a)). The attempted intervention was merely a substitute for an injunction action that the Commission might otherwise have brought against the debtor (see Section 20(b) of the Securities Act, 15 U.S.C. 77t(b)) had the latter not been under the exclusive jurisdiction of the bankruptcy court.

In short, the possibility that the district court may improvise some protective procedures in a particular case is not an adequate substitute for the many specific protections which Chapter X provides in all cases. *Amici's* contention implies that it is appropriate for the district courts to devise on a case-by-case basis procedures for corporate reorganization which may then be employed as a substitute for mandatory procedures that Congress has specified in Chapter X.

The *amici* also contend (Br. 12-13) that the failure of the proposed plan of arrangement to provide "fair and equitable" treatment to the public investors-creditors is not a proper factor to be considered in determining whether transfer to Chapter X was required, on the ground that that issue may be raised only upon review, of an order confirming the plan.* This contention misconceives the basic thrust of our argument on the "fair and equitable" point. Since the "fair and equitable" requirement was deleted from Chapter XI in 1952, it is obvious that a plan of adjustment under that Section could not be attacked for failing to meet that standard.* That is

* In *In re Lea Fabrics*, 272 F. 2d 769 (C.A. 3), to which the *amici* refer (Br. 12), the Commission did not seek review of the order confirming the plan, but only of the order denying its motion to transfer the proceedings to Chapter X.

* *Amici* argue (Br. 15, fn. 5) that the 1952 amendments "were far from 'uncontroversial.'" The only legislative history cited is the Treasury Department's objection that the deletion of the fair and equitable requirement from Chapter XI might "impair the requirement for the deposit of the moneys necessary to pay priority claims (including taxes)." H. Rep. 2320, 82d Cong., 2d Sess., p. 21. This hardly seems relevant to the points here being considered. *Amici* also refer to "examples in 9 *Collier on Bankruptcy* (14th Ed.) § 9.18(2.1) pp. 304-

precisely the reason why, in our view, transfer is required to Chapter X. In other words, since the rights of public investor-creditors cannot be adjusted in reorganization proceedings unless they receive full compensatory treatment before junior interests may participate (see our main brief, pp. 39-40), the fact that Chapter XI no longer requires that they be given such treatment is the very reason why any proceeding in which their rights are adjusted must be transferred to Chapter X, where the "fair and equitable" standard still applies.

CONCLUSION

For the foregoing reasons and those set forth in our main brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

ARCHIBALD COX,

Solicitor General.

DANIEL M. FRIEDMAN,

Assistant to the Solicitor General.

PHILIP A. LOOMIS, Jr.,

General Counsel,

DAVID FERBER,

Solicitor,

DONALD R. JOLLIFFE,

Attorney,

Securities and Exchange Commission.

NOVEMBER 1964.

"305)" but the references there are to a law review comment published ten years before the amendment (51 Yale L. J. 253, 275) and to a commentary discussing the legislation after it had been enacted (Seligson, *Bankruptcy*, 1952, Ann. Survey of American Law, 467).

APPENDIX A

**OUTCOME OF PROCEEDINGS SINCE JULY 1, 1953 IN WHICH
COMMISSION MOTIONS UNDER SECTION 328 OF THE
BANKRUPTCY ACT TO DISMISS HAVE BEEN GRANTED OR
DENIED**

	Motion granted	Motion denied
Total.....	14	10
Plan consummated.....	6 ¹	2 ⁴
Adjudicated bankrupt.....	3 ²	5 ⁵
Pending.....	5 ³	3 ⁶

¹ In the *Matter of Bruns Chemical Co., Inc.* (D.N.J., No. B 831-62) (Assets sold as economic unit pursuant to plan of reorganization). (Referred to in 29th Annual Report of the Securities and Exchange Commission, p. 96).

² In the *Matter of Dillibert's Leasing and Development Corporation* (E.D.N.Y., No. 63 B 148) (Assets liquidated pursuant to plan of reorganization). (Referred to in 29th Annual Report, p. 96).

³ In the *Matter of Dillibert's Quality Supermarkets, Inc.* (E.D.N.Y., No. 62 B 920) (Assets sold as economic unit pursuant to plan of reorganization). (Referred to in 29th Annual Report, p. 96.)

⁴ In the *Matter of General Stores Corporation* (S.D.N.Y. No. 80864). (Referred to in 22nd Annual Report, pp. 178-179.)

⁵ In the *Matter of Liberty Baking Corporation* (S.D.N.Y., Civ. No. 91173) (Assets sold as economic unit pursuant to plan of reorganization). (Referred to in 22nd Annual Report, pp. 185-186.)

⁶ In the *Matter of N. O. Nelson Co.* (S. Mo., No. 12712(2)).

⁷ In the *Matter of Daejag Stores, Inc.* (S.D.N.Y., No. 62 B 147). (Referred to in 29th Annual Report, p. 102.)

⁸ In the *Matter of Daejag Stores, Inc.* (S.D.N.Y., No. 62 B 727) (No Ch. X petition filed). (Referred to in 29th Annual Report, p. 96.)

⁹ In the *Matter of Herald Radio and Electronics Corporation* (S.D.N.Y., No. 80B-468). (See 27th Annual Report, p. 136.)

¹⁰ In the *Matter of Coast Investors, Inc.* (W.D. Wash., No. 53448).

¹¹ In the *Matter of Crumpton Builders, Inc.* (M.D. Fla., No. 63 42 T) (Denial of motion reversed on appeal). (Referred to in 29th Annual Report, p. 96.).

¹² In the *Matter of Hydrocarbon Chemicals, Inc.* (S.D.N.J., No. B-743-63).

¹³ In the *Matter of Vince Corporation* (E.D. Mich., No. 63-182). (See 29th Annual Report, p. 96.)

¹⁴ In the *Matter of Yuba Consolidated Industries, Inc.* (N.D. Cal., No. 64108).

¹⁵ In the *Matter of Transvision, Inc.* (S.D.N.Y., No. 80861). (Referred to in 21st Annual Report, pp. 93-94.)

¹⁶ In the *Matter of Wilcox-Gay Corporation* (W.D. Mich., S. Div., No. 12735). (Referred to in 22nd Annual Report, p. 179.)

The annual reports of the Commission show that in the above period there were six additional Chapter XI proceedings transferred to Chapter X either following a motion made by the Commission under Section 228 which had not yet been acted upon, or after the Commission had suggested informally that Chapter X should be utilized. Five of these debtors have been reorganized under Chapter X,¹ and one debtor has been adjudicated a bankrupt.²

¹ In the Matter of Alaska Telephone Corporation (W.D. Wash., N. Div., No. 41632) (Assets sold as economic unit pursuant to plan of reorganization). (Referred to in 22nd Annual Report, p. 179.)

In the Matter of Cal-West Aviation, Inc. (N.D. Cal., No. 63708) (Assets being liquidated pursuant to plan of reorganization). (Referred to in 28th Annual Report, p. 103.)

In the Matter of Kirschner & Arnold, Inc. (E.D.N.C., No. 2878) (Assets liquidated pursuant to plan of reorganization). (Referred to in 28th Annual Report, p. 160.)

In the Matter of Pickhouse Trust Deed Corporation (N.D. Cal., N. Div., No. 57489) (Assets liquidated pursuant to plan of reorganization). (Referred to in 28th Annual Report, p. 189.)

In the Matter of Trustees' Corporation (S.D. Cal., No. 123, 776-Y) (Assets being liquidated pursuant to plan of reorganization). (Referred to in 27th Annual Report, p. 187.)

² In the Matter of Precision Transformer Corporation (N.D. Ill., No. 62 B 2032). (Referred to in 28th Annual Report, p. 97.)

¹ In the Matter of Griggs-Robinson Stores, Inc. (S.D. N.Y., No. 62 B-584) (Debtor's application for bankruptcy adjudication pending). (Referred to in 29th Annual Report, pp. 94-95.)

In the Matter of Lee Fabrics, Inc. (D.N.J., No. 4386). (See 28th Annual Report, pp. 189-190.)

In the Matter of Life and Industrial Companies, Inc. (E.D. Ark., No. LR 66B-177). (See 27th Annual Report, pp. 126-128.)

In the Matter of Los Angeles Trust Deed & Mortgage Exchange (S.D. Cal., No. 118, 179-Y). (See 28th Annual Report, p. 188.)

In the Matter of United Star Companies, Inc. (M.D. Fla., No. 63-4-BK-T) (Appeal pending). (Referred to in 28th Annual Report, p. 97.)

² In the Matter of American Guaranty Corporation (D.C.B.I., No. 63 B 17). (See 28th Annual Report, pp. 96-98.)

In the Matter of American Trailer Rentals Company (D. Colo., No. 33276). (See 29th Annual Report, p. 98.)

In the Matter of Canadair Enterprises Corporation (W.D. N.Y., No. 5K-631954).

APPENDIX B

S.E.C.

Ex E

3-8-63

THIS AGREEMENT, made and entered this 24 day of MARCH, 1961 by and between ~~PATRICK~~ and/or JULIA BOHL hereinafter referred to as lessor and NORTH DAKOTA TRAILER RENTALS CO., a corporation organized under and existing by virtue of the laws of the State of North Dakota, hereinafter referred to as lessee; Witnesseth

1. That lessor in consideration of the covenants and agreements on the part of the lessee herein contained, does hereby lease to the lessee certain utility trailers described as follows:

Number: 1.

Size: 5'x12'

Type: Closed; all steel; 4 wheel moving vans.

Manufacturer: Demor Tra.

Serial No.: 3203-7-OBK.

together with such accessory equipment such as hitches, tarps, etc., delivered by the manufacturer as accessory parts, for use by lessee in its trailer rental system.

2. The leased trailers shall at all times remain and be the sole and exclusive property of the lessor and the lessee shall have no right in them, except as herein granted.

3. The lessee shall at all times and at his own expense keep the leased trailers in good and efficient working order and shall not permit anyone to deface or damage any of said trailers.

4. Lessor shall pay sales tax, if any, due upon purchase of said trailers, and all applicable license fees, taxes or permits required by any state or governmental authority for the purpose of permitting lessor's trailers to be operated upon public highways under the jurisdiction of such governmental authority. Lessee will procure said license and/or permits annually and deduct the amount of the fees thereof from rental due hereunder.

5. As rental for said trailer, lessee shall pay lessor 2% per month of the total dollars invested in trailers, in the amount of \$22.36 monthly or the sum of \$— quarterly for as long as this agreement remains in effect. Said payments to commence at the end of the first month (or quarter) following the effective date of this lease.

6. Said trailers have not been delivered to lessor by manufacturer and lessor cannot make delivery until receipt from the manufacturer. The effective date of this lease is the first day of the first month after notification by lessor or his agent that said trailers are ready for delivery to lessee. For this purpose, lessee is authorized to complete this lease by inserting the effective date first hereinabove provided for. The lessee is also authorized to insert the serial numbers of said trailers after notification of the same. Upon completion, lessee will provide lessor a completed copy of this lease executed by the executive officers of the company.

7. The term of this lease is for ten years from the effective date hereof, and at least 90 days prior to the expiration of this lease lessor will notify lessee which of the following options lessor will exercise:

A. Sell said trailers to lessee for 20% (\$223.62) of lessor's original purchase price which amount, together with sufficient additional monies to make

the purchase, shall be used to purchase new trailers to be leased to lessees upon a similar lease arrangement as herein set forth upon forms then in use by the lessee at rental rates then being offered by the lessee for like trailers.

B. Sell said trailers to lessees for 10% (\$111.81) of lessor's original purchase price.

C. Lessor may leave trailers in system for life time of trailers on a percentage basis of 30% of earnings after operational costs.

D. Take possession of said trailers at the nearest Central Exchange of lessee. Lessor shall have five days from the date of the expiration of this lease to remove said trailers from the premises of said Central Exchange and upon failure to remove in this time, shall subject said lessor and trailers to a reasonable storage charge thereafter.

8. Lessee shall maintain insurance upon said trailers in amounts sufficient to compensate lessor in the event of theft, damage or destruction, and in any of these events, the claim therefore shall be prosecuted by the lessee in its own name. In the event of damage, recovery of claim shall be applied to repair of said trailers. In the event of total destruction or theft, this lease will terminate as to such trailer and shall pay lessor the value of such trailer. Initial insured value shall be the purchase price of the trailer. Thereafter the insured value shall be reduced annually by 15% of the valuation of the preceding year for the term of this lease. Lessee will maintain comprehensive liability and property damage insurance that will save lessor harmless in case of accident.

9. Lessor shall at all times have the right to sell or transfer or assign his title to said trailers subject to this agreement or to sell or assign his rights and benefits under this agreement.

10. This lease is executed to cover more than one trailer, but a separate lease shall be prepared for each trailer covered by this multiple lease and upon execution of said separate lease agreements, said leases shall supersede this lease agreement.

IN WITNESS WHEREOF, the parties hereto have duly executed this instrument in duplicate this 24th day of March, 1961.

PETER BOHL,
JULIA BOHL,

Lessor.

NORTH DAKOTA TRAILER RENTALS Co.
By ALVIN MOLZIN.